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Accounting and Financial Management for Bankers

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ACCOUNTING & FINANCIAL MANAGEMENT FOR BANKERS

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JAIIB Accounting and Financial Management for Bankers
Chapterwise Question Bank
Edition January 2026
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125, Sector 6, Vidyadhar Nagar, Jaipur 302039
Phone :+91 9024037387
email : mail@nodia.in

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CHAPTER 1

Definition, Scope & Accounting Standards Including Ind As

Oct/Nov 2015

1. According to the 'American Institute of Certified Public Accountants' (AICPA), which of the following is NOT considered a primary function within the art of accounting?

(A) Recording transactions and events in terms of money.

(B) Auditing the financial statements for regulatory compliance.

(C) Classifying financial transactions in a significant manner.

(D) Summarising financial data to produce financial statements.

Ans :

(B) Auditing the financial statements for regulatory compliance.

The AICPA definition of accounting describes it as the art of recording, classifying, and summarising transactions and events of a financial character, and interpreting the results thereof. Auditing, while related to accounting, is a separate process of examining financial records to ensure their accuracy and compliance, not a core function within the definition of accounting itself.

May/June 2008

2. Which statement best distinguishes between bookkeeping and accountancy?

(A) Bookkeeping involves recording transactions, while accountancy is a wider concept that includes compilation and interpretation of accounts.

(B) Bookkeeping is the final, analytical stage of accounting, involving the complex interpretation of financial data for strategic decisions.

(C) Accountancy is a narrower concept than bookkeeping, focused solely on the mechanical task of recording transactions in ledgers.

(D) Bookkeeping and accountancy are interchangeable terms for the same comprehensive process, covering everything from recording to interpretation.

Ans :

(A) Bookkeeping involves recording transactions, while accountancy is a wider concept that includes compilation and interpretation of accounts.

Bookkeeping is primarily concerned with the mechanical task of recording business transactions in the books of original entry and ledgers. Accountancy is a much broader concept which encompasses not only bookkeeping but also the systematic compilation and interpretation of accounts to understand the financial state of the business, making it a more comprehensive and analytical process.

Oct/Nov 2024

3. Which of the following is typically NOT included in the composition of financial statements?

(A) Balance sheet and profit and loss account.

(B) Statement of changes in financial position, such as a cash flow statement.

(C) Internal management reports on employee productivity.

(D) Explanatory statements, notes, and schedules forming part of the financial statement.

Ans :

(C) Internal management reports on employee productivity.

Financial statements normally include the balance sheet, profit and loss account, a statement of changes in financial position (like a fund flow or cash flow statement), and related explanatory notes and schedules. Internal reports on non-financial metrics like employee productivity, while useful for management, are not considered

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a standard component of the formal financial statements provided to external users.

May/June 2019

4. What is the primary objective of financial statements?

(A) To provide information focused solely on the needs of the income tax department for annual tax liability calculation.

(B) To list all the physical assets owned by a business, such as land and machinery, without assigning corresponding monetary values.

(C) To communicate the company's detailed marketing and new product strategies to potential investors and business associates.

(D) To provide information about the financial position, performance, and changes in financial position of an enterprise.

Ans :

(D) To provide information about the financial position, performance, and changes in financial position of an enterprise.

The main objective of financial statements is to offer structured information regarding an enterprise's financial standing (assets, liabilities, equity), its performance (profits, losses), and shifts in its financial position. This information is crucial for a wide range of users, including investors, creditors, and government authorities, to make informed economic decisions about the entity.

Oct/Nov 2011

5. The set of rules and criteria that govern the recording of events in accounts, analogous to grammar in a language, are known as:

(A) Accounting Procedures.

(B) Accounting Manuals.

(C) Accounting Standards.

(D) Accounting Conventions.

Ans :

(C) Accounting Standards.

Just as a language has a set of rules called grammar to ensure clarity and consistency, the process of recording financial events follows its own set of rules and criteria. These established rules are known as 'Accounting Standards' (AS). They are designed to ensure that financial statements exhibit a 'true and fair' view of an entity's financial affairs.

May/June 2025

6. Consider the following processes involved in accountancy:

1. Recording of events and transactions, known as bookkeeping.
2. Systematic classification of business transactions for recording.
3. Interpreting financial transactions from recorded data.

What is the correct sequence of these processes?

(A) 1, 2, 3

(B) 2, 1, 3

(C) 3, 2, 1

(D) 1, 3, 2

Ans :

(B) 2, 1, 3

The accountancy process follows a logical sequence. It begins with the systematic classification of business transactions. This is followed by the recording of these transactions, which is called bookkeeping. The final step involves summa rising the recorded data and interpreting the financial information to understand the business's performance and position, which aids in decision-making.

Oct/Nov 2006

7. Which feature of accounting explains why a quarrel between management and workers is not recorded in the books, but any monetary loss resulting from it is?

(A) Accounting is an art of summa rising business transactions.

(B) Accounting also interprets the financial data.

(C) Accounting records only transactions of a non-financial character.

(D) Accounting records the transactions in terms of money.

Ans :

(D) Accounting records the transactions in terms of money.

A core feature of accounting is the money measurement principle. It dictates that only transactions and events that can be expressed in monetary terms are recorded. Therefore, a non-monetary event like a quarrel is ignored, but if it leads to a quantifiable monetary outflow or loss, that financial impact will be recorded in the books of account.

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May/June 2012

8. A company purchases a high-speed computer for ₹1 lakh. Based on the features of accounting, what will be recorded in the books of account?
(A) The computer's cost price of ₹1 lakh.
(B) The computer's high efficiency and brand name.
(C) The expected increase in productivity from using the computer.
(D) A qualitative note about the computer's advanced technology.

Ans :

(A) The computer's cost price of ₹1 lakh.
Accounting records only those aspects of a transaction that are financial in character. While the computer's efficiency and brand are important business attributes, they cannot be expressed in monetary terms. Therefore, the accounting entry will only capture the financial aspect of the transaction, which is the cost price of ₹1 lakh paid for the asset.

Oct/Nov 2017

9. Which of the following is NOT listed as a primary purpose of accountancy?
(A) To ascertain the results of operations.
(B) To keep a systematic record of transactions.
(C) To determine the market share of the business.
(D) To ascertain the financial position of the business.

Ans :

(C) To determine the market share of the business.
The primary purposes of accountancy include keeping systematic records, ascertaining profit or loss, determining the financial position (assets and liabilities), facilitating rational decision-making, and satisfying legal requirements. Determining market share is a function of marketing and market research, not a direct purpose of the financial accounting process, although accounting data can indirectly support this analysis.

May/June 2005

10. Financial statements are often referred to as the "barometers of health of a business entity." This analogy implies that they:
(A) reveal the financial health and strength of an organization.
(B) can predict future economic conditions with perfect accuracy.
(C) are complex and can only be understood by medical professionals.
(D) only measure the business's performance during profitable periods.

Ans :

(A) reveal the financial health and strength of an organization.
This analogy suggests that just as a barometer indicates atmospheric pressure, financial statements indicate the financial health of a business. By examining statements like the balance sheet, a user can assess the entity's financial strength, including its position of assets, liabilities, and cash availability, much like a doctor assesses a person's health by checking their pulse.

Oct/Nov 2012

11. Which of the following statements about the advantages of financial accounting is incorrect?
(A) It provides information useful for making economic decisions.
(B) It supplies information for judging management's ability to utilize enterprise resources effectively.
(C) It provides information useful to investors for predicting and comparing cash flows.
(D) It serves primarily those users who have unlimited authority and resources to obtain information.

Ans :

(D) It serves primarily those users who have unlimited authority and resources to obtain information.
Financial accounting primarily serves users who have limited authority, ability, or resources to obtain information directly from the enterprise. These users, such as external investors and creditors, rely on general-purpose financial statements as their principal source of economic information. Users with unlimited authority, like top management, can access more detailed internal reports.

May/June 2016

12. The evolutionary phase of accounting that is associated with wealthy people employing 'stewards' to manage their property and render periodic accounts is known as:
(A) Financial Accounting.

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(B) Stewardship Accounting.
(C) Management Accounting.
(D) Cost Accounting.

Ans :

(B) Stewardship Accounting.
Stewardship accounting is the earliest phase in the evolution of accounting. It originated from the practice where wealthy owners employed stewards to manage their properties. These stewards were accountable to the owners and had to periodically report on their management of the assets. This concept of accountability is the historical root of modern financial reporting.

Oct/Nov 2021

13. The 'double entry bookkeeping' method, which forms the basis of modern accounting, has its origins in the practices employed by merchants in which country during the fifteenth century?
(A) England.
(B) Greece.
(C) Italy.
(D) Holland.

Ans :

(C) Italy.
The systematic recording of business transactions using the double-entry method originated with merchants in Italy during the fifteenth century. This Italian method was a significant development in the history of accounting, and its principles were later adopted across Europe and the world, forming the foundation of contemporary accounting practices.

May/June 2023

14. The advent of which form of business organisation was a major driver for the development of Financial Accounting?
(A) Sole Proprietorship.
(B) Partnership Firms.
(C) Barter System.
(D) Joint Stock Companies.

Ans :

(D) Joint Stock Companies.
The development of financial accounting is closely linked to the rise of large-scale business and the 'Joint Stock Company' structure. This business form allows public participation through capital investment in shares and limits shareholder liability. This created a crucial need for reliable financial reporting to inform these external investors about the company's performance and financial position.

Oct/Nov 2009

15. What is the most significant social purpose of financial accounting?
(A) To provide reliable information to investors for making efficient investment decisions.
(B) To ensure all companies pay the maximum amount of tax to the government.
(C) To help company directors conceal information from the public and competitors.
(D) To replace the need for all other types of accounting like cost and management accounting.

Ans :

(A) To provide reliable information to investors for making efficient investment decisions.
The most significant social purpose of financial accounting is to support the efficient functioning of capital markets. By providing reliable and sufficient information, it enables society to mobilise savings and channel them into profitable investments. This allows both large and small investors to make informed and efficient decisions, fostering economic growth and stability.

May/June 2011

16. Which historical event presented a major challenge that led to the development of Cost Accounting as a tool for industrial management?
(A) The Italian Renaissance.
(B) The Industrial Revolution in England.
(C) The formation of Joint Stock Companies.
(D) The World Wars of the twentieth century.

Ans :

(B) The Industrial Revolution in England.
The Industrial Revolution in England brought about large-scale factory production and complex manufacturing processes. This created a pressing need for managers to understand, control, and analyze the costs of production. As a result, cost accounting techniques were developed to ascertain the cost of products and departments, assess profitability, and improve efficiency in industrial management.

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Oct/Nov 2022

17. A key difference between Management Accounting and Financial Accounting is that Management Accounting is:
(A) primarily historical, focusing on recording past transactions for external reporting.
(B) forward-looking and not constrained by legal regulations or accounting standards.
(C) strictly bound by legal regulations and generally accepted accounting principles.
(D) focused on providing information to external stakeholders like investors and creditors.

Ans :

(B) forward-looking and not constrained by legal regulations or accounting standards.
Management accounting is primarily forward-looking, designed to aid internal management in policy formulation and decision-making for the future. Unlike financial accounting, which is historical and must adhere to legal rules and accounting standards, management accounting is relatively free from such constraints, allowing for more flexible and tailored reporting to meet specific managerial needs.

May/June 2013

18. Which branch of accounting widens its scope by considering the social effects of business decisions in addition to their economic effects?
(A) Social Responsibility Accounting.
(B) Human Resource Accounting.
(C) Inflation Accounting.
(D) Financial Accounting.

Ans :

(A) Social Responsibility Accounting.
Social Responsibility Accounting is a relatively new phase in accounting that extends beyond purely economic metrics. It considers and reports on the social impact of a business's operations, such as its effect on the environment, ecology, and social well-being. This reflects a growing societal expectation for businesses to be accountable for more than just their profitability.

Oct/Nov 2018

19. What is the primary focus of Human Resource Accounting (HRA)?
(A) To calculate the monthly salaries and wages of all employees in an organisation.
(B) To ensure compliance with labour laws regarding employee working hours and conditions.
(C) To report and emphasise the importance of human resources as assets in a company's earning process.
(D) To track the costs associated with employee training for tax deduction purposes only.

Ans :

(C) To report and emphasise the importance of human resources as assets in a company's earning process.
Human Resource Accounting (HRA) is a branch of accounting that seeks to identify, measure, and communicate the value of human resources to an organization. It involves accounting for the investment in people and their economic value, emphasizing that knowledgeable, trained, and loyal employees are crucial assets contributing significantly to the company's earning process and total value.

May/June 2007

20. Inflation accounting aims to correct distortions in reported results caused by price level changes by addressing limitations arising from which two assumptions of traditional accounting?
(A) Cost assumption and stable monetary unit assumption.
(B) Going concern and consistency assumptions.
(C) Accrual and periodicity assumptions.
(D) Business entity and dual aspect assumptions.

Ans :

(A) Cost assumption and stable monetary unit assumption.
Inflation accounting is concerned with overcoming the limitations of traditional financial statements during periods of changing prices. These limitations stem from the historical cost assumption (recording assets at original cost) and the stable monetary unit assumption (assuming money's purchasing power is constant). Inflation accounting adjusts asset values and profits to reflect current price levels.

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Oct/Nov 2025

21. Five workers are picking tea leaves and putting them into a single basket. An accounting system is used to track the contribution of each worker to decide their share of revenue upon sale. What is this system called?
(A) Cost Accounting.
(B) Fair Value Accounting.

(C) Inflation Accounting.
(D) Value Accounting.

Ans :

(D) Value Accounting.
Value accounting is used to evaluate and capture individual contributions, whether tangible or intangible, to a product or service. In this case, the system is tracking each worker's specific contribution to the collective output (the basket of tea leaves) to determine their respective share of the final revenue, which is the core purpose of value accounting.

May/June 2014

22. What is the primary characteristic of Fair Value Accounting?
(A) It values assets and liabilities based on their original purchase price.
(B) It takes into account the current market value of certain assets and liabilities.
(C) It is concerned with the intention of the holder to keep or sell the asset.
(D) It is widely accepted due to the high availability of reliable information.

Ans :

(B) It takes into account the current market value of certain assets and liabilities.
Fair value accounting, also known as current value accounting, measures certain assets and liabilities at their current market value. Fair value is the estimated price at which an asset could be sold or a liability settled under current market conditions. This approach is distinct from historical cost accounting, which uses the original transaction price for valuation.

Oct/Nov 2014

23. The book 'Summa', which contained a section on 'Double Entry' bookkeeping, was published in 1494 by an Italian monk named:
(A) Kautilya.
(B) Francis Wheat.
(C) Luca De Bargo Pacioli.
(D) Hermansson.

Ans :

(C) Luca De Bargo Pacioli.
In 1494, at Venice, the Italian monk Luca De Bargo Pacioli published his influential book titled 'Summa'. This work included a detailed section on the principles of 'Double Entry' bookkeeping. Its publication and subsequent use by merchants were pivotal in the standardization and spread of modern accounting methods across Europe.

May/June 2021

24. In India, the ancient book on accountancy written by Kautilya during the regime of King Chandragupta was named:
(A) Summa.
(B) Nama.
(C) Deshi.
(D) Arthashastra.

Ans :

(D) Arthashastra.
Accountancy was practiced in a scientific form in India as far back as twenty centuries ago. During the reign of King Chandragupta, his minister Kautilya authored a book on statecraft, economic policy, and military strategy named the 'Arthashastra', which also discussed the critical role of accounting and record-keeping in society and governance.

Oct/Nov 2010

25. The Accounting Standards Board (ASB) was constituted by the Institute of Chartered Accountants of India (ICAI) on which date?
(A) 21st April, 1977
(B) 15th June, 2001
(C) 1st April, 2001
(D) 1st October, 2018

Ans :

(A) 21st April, 1977
Recognizing the need to harmonize the diverse accounting policies and practices prevalent in India, the Institute of Chartered Accountants of India (ICAI) took a significant step by constituting the 'Accounting Standards Board' (ASB) on 21st April, 1977. The primary function of the ASB is to formulate accounting standards for mandatory application.

May/June 2018

26. What is the final step in the procedure for formulating accounting standards by the ASB before a standard is issued?
(A) The ASB determines the broad areas for which standards are needed.
(B) The council of ICAI considers the final draft, modifies it if necessary, and issues the standard.

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(C) An exposure draft is prepared and issued for public comment.
(D) Study groups are constituted to consider specific subjects and hold dialogues with industry.

Ans :

(B) The council of ICAI considers the final draft, modifies it if necessary, and issues the standard.
The formulation process is multi-staged, starting with area identification, followed by study group work and the creation of an exposure draft for public comment. After comments are considered, the ASB finalizes the draft and submits it to the council of ICAI. The final step is the council's consideration and potential modification before it is officially issued.

Oct/Nov 2016

27. Under Section 129(5) of the Companies Act 2013, if a company's financial statements do not comply with accounting standards, which disclosure is NOT required?
(A) The deviation from the accounting standards.
(B) The names of the board members who approved the deviation.
(C) The reasons for such a deviation.
(D) The financial effects, if any, arising out of such a deviation.

Ans :

(B) The names of the board members who approved the deviation.
Section 129(5) of the Companies Act, 2013 mandates specific disclosures in case of non-compliance with accounting standards. The company must disclose the deviation itself, the reasons for it, and the resulting financial effects. However, the act does not explicitly require the disclosure of the names of the specific board members who approved this deviation.

May/June 2024

28. Which body, constituted under Section 132 of the Companies Act, 2013, has replaced the 'National Advisory Committee on Accounting Standards' and acts as an independent audit regulator?
(A) National Financial Reporting Authority (NFRA).
(B) Accounting Standards Board (ASB).
(C) Institute of Chartered Accountants of India (ICAI).
(D) Securities and Exchange Board of India (SEBI).

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Ans :

(A) National Financial Reporting Authority (NFRA).
The National Financial Reporting Authority (NFRA) was constituted effective from 1st October 2018 under the Companies Act, 2013. It replaced the previous National Advisory Committee on Accounting Standards. NFRA is an independent regulatory body that assists in framing and enforcing legislation related to accounting and auditing, and it oversees the profession, including the ICAI.

Oct/Nov 2007

29. Which Accounting Standard deals with 'Revenue Recognition'?
(A) AS 7 (Revised)
(B) AS 10 (Revised)
(C) AS 9
(D) AS 12

Ans :

(C) AS 9
According to various lists of Accountancy Standards, AS 9 is explicitly titled 'Revenue Recognition'. AS 7 deals with Construction Contracts, AS 10 with Property, Plant and Equipment, and AS 12 with Accounting for Government Grants.

May/June 2009

30. Match the Accounting Standard (List-I) with its corresponding title (List-II).
List-I (AS Number)
P. AS 2 (Revised)
Q. AS 3 (Revised)
R. AS 16
S. AS 18
List-II (Title)
1. Borrowing Costs
2. Related Party Disclosures
3. Valuation of Inventories
4. Cash Flow Statements
(A) P-3, Q-4, R-1, S-2
(B) P-4, Q-3, R-2, S-1
(C) P-3, Q-1, R-4, S-2
(D) P-2, Q-4, R-1, S-3

Ans :

(A) P-3, Q-4, R-1, S-2

As per the generally accepted list of Accountancy Standards, AS 2 (Revised) corresponds to Valuation of Inventories. AS 3 (Revised) is for Cash Flow Statements. AS 16 deals with Borrowing Costs, and AS 18 is for Related Party Disclosures. Therefore, the correct matching is P with 3, Q with 4, R with 1, and S with 2.

Oct/Nov 2019

31. What is the title of Accounting Standard 22 (AS 22)?
(A) Leases
(B) Earnings Per Share
(C) Consolidated Financial Statements
(D) Accounting for Taxes on Income

Ans :

(D) Accounting for Taxes on Income
The table of Accountancy Standards clearly lists the title for AS 22 as 'Accounting for Taxes on Income'. This standard addresses the complexities that arise from differences between accounting income and taxable income.

May/June 2010

32. From the list of Accounting Standards, identify the incorrect pair of AS number and its title.
(A) AS 24: Discontinuing Operations
(B) AS 29: Financial Reporting of Interests in Joint Ventures
(C) AS 26: Intangible Assets
(D) AS 28: Impairment of Assets

Ans :

(B) AS 29: Financial Reporting of Interests in Joint Ventures
According to the standard list, AS 29 is titled 'Provisions, Contingent Liabilities and Contingent Assets'. The standard 'Financial Reporting of Interests in Joint Ventures' is AS 27. Therefore, the pair 'AS 29: Financial Reporting of Interests in Joint Ventures' is incorrect. The other pairs correctly match the AS number with its respective title.

Oct/Nov 2013

33. What is the main purpose of Accounting Standard-1 (AS-1) on Disclosure of Accounting Policies?
(A) To mandate specific accounting policies for all enterprises to ensure uniformity.
(B) To list all possible accounting policies an enterprise can choose from without any restrictions.
(C) To promote a better understanding of financial statements and facilitate meaningful comparison between different enterprises.
(D) To require disclosure only when fundamental accounting assumptions like going concern are not followed.

Ans :

(C) To promote a better understanding of financial statements and facilitate meaningful comparison between different enterprises.
The primary purpose of AS-1 is not to enforce uniform policies but to ensure transparency by requiring disclosure of the significant accounting policies followed. This disclosure helps users better understand the financial statements and allows for a more meaningful comparison between the financial statements of two different enterprises, which may have adopted different accounting policies in certain areas.

May/June 2020

34. Consider the following statements:
Statement I : According to AS-1, if fundamental accounting assumptions like going concern, consistency, and accrual are followed, a specific disclosure is required.
Statement II : According to AS-1, any change in an accounting policy that has a material effect in the current period should be disclosed.
(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Statement I is correct, but Statement II is incorrect.
(D) Statement I is incorrect, but Statement II is correct.

Ans :

(D) Statement I is incorrect, but Statement II is correct.
AS-1 states that if the fundamental accounting assumptions (going concern, consistency, accrual) are followed, specific disclosure is not required; it is assumed they are followed. Disclosure is only needed if they are not followed. However, AS-1 does mandate that any change in accounting policy with a material effect must be disclosed, making Statement II correct.

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Oct/Nov 2005

35. As per Accounting Standard-2 (Revised), inventories should be valued at:
(A) Lower of cost or net realisable value.
(B) Cost or net realisable value, whichever is higher.
(C) Only the cost of the inventories.
(D) Only the net realisable value of the inventories.

Ans :

(A) Lower of cost or net realisable value.
A fundamental principle prescribed by AS-2 (Revised) is the rule of prudent valuation for inventories. The standard mandates that inventories must be valued at the lower of their historical cost or their net realisable value (NRV). This ensures that assets are not overstated and that any potential losses are recognised in the period they occur.

May/June 2017

36. Accounting Standard-2 (Revised) on valuation of inventories is NOT applicable to which of the following?
(A) Raw materials waiting to be used in production.
(B) Work in progress arising under construction contracts.
(C) Finished goods held for sale in the ordinary course of business.
(D) Consumable stores and spares.

Ans :

(B) Work in progress arising under construction contracts.
AS-2 (Revised) explicitly states that it does not apply to certain items. Among the exclusions is work in progress that arises under construction contracts, as this is specifically covered by another standard, AS-7 (Revised) on Construction Contracts. It also excludes items like financial instruments held as stock-in-trade and inventories of livestock and agricultural products.

Oct/Nov 2020

37. According to AS-3, cash flows in a cash flow statement are required to be classified into which three heads?
(A) Operational, Managerial, and Administrative activities.
(B) Inflow, Outflow, and Net-flow activities.
(C) Current, Non-current, and Contingent activities.
(D) Operating, Investing, and Financing activities.

Ans :

(D) Operating, Investing, and Financing activities.
Accounting Standard-3 mandates the classification of cash flows into three distinct categories to provide clear insights into an enterprise's liquidity and solvency. These categories are Operating activities (principal revenue-producing activities), Investing activities (acquisition and disposal of long-term assets), and Financing activities (transactions related to owner's capital and borrowings).

May/June 2006

38. As per AS-3, an investment with a short maturity of, say, 3 months or less from the date of acquisition, which is readily convertible into a known amount of cash, is known as a:
(A) Current asset.
(B) Cash equivalent.
(C) Short-term investment.
(D) Demand deposit.

Ans :

(B) Cash equivalent.
AS-3 defines cash equivalents as short-term, highly liquid investments that are readily convertible into a known amount of cash and are subject to an insignificant risk of changes in value. An investment typically qualifies as a cash equivalent only when it has a short maturity, generally considered to be three months or less from its acquisition date.

Oct/Nov 2008

39. A company's financial statements are to be approved by the Board of Directors on May 15th. The balance sheet date is March 31st. On April 20th, a major debtor of the company declares insolvency. According to AS-4 (Revised), how should this event be treated?
(A) The event should be ignored as it occurred after the balance sheet date.
(B) The event should only be disclosed in the director's report, not in the financial statements.
(C) The assets and liabilities should be adjusted as it provides evidence of conditions existing

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at the balance sheet date.
(D) A provision should be made only if the financial statements are approved after June 30th.

Ans :

(C) The assets and liabilities should be adjusted as it provides evidence of conditions existing at the balance sheet date.
AS-4 deals with events occurring after the balance sheet date. The insolvency of a debtor post-balance sheet date confirms that the loss on the receivable amount was a condition that already existed on the balance sheet date (i.e., the debt was already doubtful). Therefore, this is an adjusting event, requiring the adjustment of assets and liabilities.

May/June 2015

40. Under AS-4 (Revised), how is a contingent gain typically treated in the financial statements?
(A) It is not recognised, but when its realisation is virtually certain, it is accounted for as income.
(B) It is recognised as income if its realisation is probable.
(C) It is recognised as income only when it is received.
(D) It is not recognised, but may be disclosed if inflow of benefits is probable.

Ans :

(A) It is not recognised, but when its realisation is virtually certain, it is accounted for as income.
The principle of prudence under AS-4 dictates that contingent gains should not be recognised in financial statements to avoid booking income that may never be realised. However, if the realisation of the gain becomes virtually certain, it ceases to be a contingency. At that point, it is no longer a contingent gain and is appropriately recognised as income.

Oct/Nov 2023

41. According to AS-5 (Revised), incomes or expenses that arise in the current period as a result of errors or omissions in the preparation of financial statements of one or more prior periods are defined as:
(A) Extraordinary items.
(B) Changes in accounting estimates.
(C) Ordinary activities.
(D) Prior period items.

Ans :

(D) Prior period items.
AS-5 defines prior period items specifically as incomes or expenses that arise in the current accounting period due to mistakes or omissions made during the preparation of the financial statements for previous periods. These are corrected by restating the comparative amounts for the prior period(s) presented in which the error occurred.

May/June 2022

42. Which statement accurately describes the treatment of 'Extraordinary Items' under AS-5 (Revised)?
(A) They are common events that are part of the day-to-day activities of an enterprise.
(B) They are incomes or expenses arising from events that are clearly distinct from ordinary activities and not expected to recur.
(C) They are not required to be disclosed separately in the financial statements.
(D) They are identical to prior period items and treated in the same manner.

Ans :

(B) They are incomes or expenses arising from events that are clearly distinct from ordinary activities and not expected to recur.
AS-5 defines extraordinary items as those that are clearly distinct from the ordinary activities of the business. Their key characteristics are that they are not expected to recur frequently or regularly. Due to their unusual nature and potential to distort the understanding of an enterprise's performance, they must be disclosed separately in the financial statements.

Oct/Nov 2015

43. Under AS-7 (Revised), which accounting method for construction contracts is based on the proportion of contract work performed during a period?
(A) The completed contract method.
(B) The cost plus contract method.
(C) The percentage of completion method.
(D) The fixed price contract method.

Ans :

(C) The percentage of completion method.
AS-7 recognizes two primary methods for contract accounting. The percentage of completion

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method involves recognizing revenue, costs, and profit in proportion to the stage of completion of the contract work. This contrasts with the completed contract method, where revenue and profit are only recognized after the contract is fully or substantially completed.

May/June 2008

44. Accounting Standard-9 on Revenue Recognition does not deal with revenue arising from which of the following?
(A) Sale of goods.
(B) Rendering of services.
(C) Use of enterprise resources yielding interest and dividends.
(D) Construction contracts.

Ans :

(D) Construction contracts.
AS-9 provides guidance on when to recognise revenue from various activities like the sale of goods, rendering of services, and from interest, royalties, and dividends. However, it explicitly states that it does not apply to revenue arising from construction contracts, as this is specifically addressed in detail by Accounting Standard-7 (Revised).

Oct/Nov 2024

45. According to AS-10 (Revised 2016), the cost of an item of Property, Plant, and Equipment (PPE) should be recognised as an asset if and only if:
(A) It is probable that future economic benefits will flow to the enterprise, and the cost can be measured reliably.
(B) The cost of the item can be measured reliably, and it is tangible.
(C) The item is expected to be used for more than one year and is for administrative purposes.
(D) The purchase has been approved by the board of directors, and it is held for production.

Ans :

(A) It is probable that future economic benefits will flow to the enterprise, and the cost can be measured reliably.
AS-10 specifies two crucial criteria for the recognition of an item as PPE. First, it must be probable that the future economic benefits associated with the asset will flow to the entity. Second, the cost of acquiring the asset must be capable of being measured reliably. Both conditions must be met for the item to be capitalized.

May/June 2019

46. As per the exclusions listed under AS-10, which of the following costs should NOT be included in the cost of an item of PPE?
(A) Costs of site preparation.
(B) Costs of opening a new facility, such as inauguration costs.
(C) Installation and assembly costs.
(D) Costs of testing whether the asset is functioning properly.

Ans :

(B) Costs of opening a new facility, such as inauguration costs.
AS-10 explicitly lists costs that are excluded from the initial cost of an item of PPE. These include administration and general overheads, costs of opening a new facility (like inauguration costs), and costs of introducing a new product. Costs like site preparation, installation, and testing are considered directly attributable and are included in the asset's cost.

Oct/Nov 2011

47. A company acquires an item of PPE under a deferred payment plan. The total payment is ₹1,20,000, while the cash price equivalent is ₹1,00,000. How should the difference of ₹20,000 be treated under AS-10?
(A) It should be recognised as interest over the period of credit.
(B) It should be added to the cost of the PPE.
(C) It should be written off immediately as an expense in the year of purchase.
(D) It should be ignored for accounting purposes.

Ans :

(A) It should be recognised as interest over the period of credit.
AS-10 specifies that when PPE is acquired under a deferred payment plan, the difference between the total payment and the cash price equivalent represents a financing cost. This difference should be recognized as interest expense over the credit period, unless it qualifies for capitalization under AS 16, Borrowing Costs. It is not part of the asset's initial cost.

May/June 2025

48. Consider the following statements:

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Statement I : Under the revaluation model in AS-10, an increase in an asset's carrying amount is always credited to the Statement of Profit and Loss.

Statement II : Under the revaluation model in AS-10, a decrease in an asset's carrying amount is always debited to the Statement of Profit and Loss.

(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Statement I is correct, but Statement II is incorrect.
(D) Statement I is incorrect, but Statement II is correct.

Ans :

(B) Both Statement I and Statement II are incorrect.

An increase from revaluation is credited to a 'revaluation surplus' under owners' interests, not the P&L, unless it reverses a previous decrease. A decrease is charged to the P&L, but if a revaluation surplus exists for that asset, the decrease is first debited against that surplus. Therefore, neither statement is universally correct.

Oct/Nov 2006

49. What does AS-11 (Revised 2018) primarily deal with?
(A) The accounting for government grants and subsidies.
(B) The methods of depreciation for property, plant, and equipment.
(C) The accounting for transactions in foreign currencies and translation of foreign operations.
(D) The recognition of revenue from the sale of goods.

Ans :

(C) The accounting for transactions in foreign currencies and translation of foreign operations.

AS-11 (Revised 2018) provides comprehensive guidance on accounting for foreign currency transactions. This includes how to record transactions denominated in a foreign currency and how to translate the financial statements of a foreign branch or operation into the reporting currency of the parent company, along with the treatment of resulting exchange differences.

May/June 2012

50. In the context of AS-11, what is 'Reporting Currency'?
(A) The currency used in presenting the financial statements.
(B) The currency of the country where the head office is domiciled.
(C) A currency other than the reporting currency of an enterprise.
(D) The currency of the primary economic environment in which the entity operates.

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Ans :

(A) The currency used in presenting the financial statements.

AS-11 defines 'Reporting Currency' as the currency in which an enterprise presents its financial statements. For an Indian company, this is typically the Indian Rupee. This is distinct from a 'Foreign Currency' (any other currency) or the 'Functional Currency' (the currency of the primary economic environment in which the entity operates).

Oct/Nov 2017

51. Accounting Standard-12 on government grants does not deal with which of the following?
(A) Cash incentives received from the government.
(B) Duty drawbacks received as a form of grant.
(C) Grants in the form of non-monetary assets at a concessional rate.
(D) Government assistance in the form of a tax holiday in backward areas.

Ans :

(D) Government assistance in the form of a tax holiday in backward areas.

AS-12 specifically excludes certain forms of government assistance from its scope, even though they are beneficial to the enterprise. One such exclusion is government assistance that affects the determination of taxable income, such as tax holidays, tax exemptions, and investment tax credits. The standard focuses on direct grants like subsidies and duty drawbacks.

May/June 2005

52. Under AS-12, when should government grants be recognised in the profit and loss statement?
(A) Immediately upon receiving the cash from the government.

(B) On a systematic and rational basis over the periods necessary to match them with the related costs.
(C) In a single lump sum in the year the grant is sanctioned, regardless of conditions.
(D) Only after all the conditions of the grant have been fulfilled for the entire grant period.

Ans :

(B) On a systematic and rational basis over the periods necessary to match them with the related costs.
The principle in AS-12 is to match the recognition of the grant income with the costs it is intended to compensate. Therefore, grants should be recognised in the profit and loss statement on a systematic basis over the periods in which the entity recognises the related costs for which the grant is meant to compensate.

Oct/Nov 2012

53. AS-13 (Revised 2016) on Accounting for Investments does not apply to which of the following entities?
(A) A manufacturing company holding shares in another company as a long-term investment.
(B) A trading company holding debentures as current investments.
(C) Mutual funds and related asset management companies.
(D) A software company that owns its office building.

Ans :

(C) Mutual funds and related asset management companies.
AS-13 explicitly states that it does not deal with the investments of certain types of enterprises, including retirement benefit plans, life insurance enterprises, mutual funds, and venture capital funds. These entities have specialized accounting requirements for their investment portfolios that are governed by industry-specific regulations and standards, not by the general principles of AS-13.

May/June 2016

54. In the context of AS-14 (Revised 2016), what is a 'transferee company'?
(A) The company which is amalgamated into another company.
(B) A company that is acquired but not dissolved.
(C) The original company before any amalgamation occurs.
(D) The company into which another company is amalgamated.

Ans :

(D) The company into which another company is amalgamated.
AS-14 defines the terminology used in amalgamations clearly. The company that gets amalgamated or merged into another is called the 'transferor company'. The company that absorbs the other company, i.e., the company into which the transferor company is amalgamated, is known as the 'transferee company'. It is the continuing or resulting entity.

Oct/Nov 2021

55. Which of the following is a key distinguishing feature of an 'amalgamation in the nature of merger' as per AS-14?
(A) It involves the pooling of assets, liabilities, and interests of the amalgamating companies.
(B) The acquired company is not dissolved and continues to exist as a separate entity.
(C) The accounting is done using the purchase method only.
(D) Any excess of consideration over net assets is treated as a deficit.

Ans :

(A) It involves the pooling of assets, liabilities, and interests of the amalgamating companies.
An amalgamation in the nature of a merger is essentially a pooling of interests where the shareholders of the amalgamating companies continue to have a proportionate share in the equity of the combined entity. This is accounted for using the 'pooling of interest method', which reflects the continuation of the existing businesses in a combined form.

May/June 2023

56. AS-15 (Revised 2005) on Employee Benefits includes all of the following EXCEPT:
(A) Short-term monetary and non-monetary benefits.
(B) Retirement benefits for which the employer's obligations cannot be reasonably estimated.
(C) Post-employment benefits like pension and gratuity.
(D) Termination benefits.

Ans :

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(B) Retirement benefits for which the employer's obligations cannot be reasonably estimated.
AS-15 covers a wide range of employee benefits, including short-term, post-employment, long-term, and termination benefits. However, the standard explicitly states that it does not apply to those retirement benefits where the employer's obligation cannot be reasonably estimated, as a reliable measurement is a prerequisite for accounting recognition and disclosure under the standard.

Oct/Nov 2009

57. Under AS-16, when should the capitalisation of borrowing costs for a qualifying asset cease?
(A) When the asset is partially completed but not yet ready for use.
(B) When substantially all the activities necessary to prepare the asset for its intended use or sale are complete.
(C) When the borrowed funds are fully repaid to the lender.
(D) When the development of the asset is temporarily interrupted for a short period.

Ans :

(B) When substantially all the activities necessary to prepare the asset for its intended use or sale are complete.
AS-16 mandates that the capitalization of borrowing costs should cease when the qualifying asset is substantially ready for its intended use or sale. This means that once the asset is in the condition to be put to use or sold, any further borrowing costs incurred should be treated as an expense in the profit and loss account.

May/June 2011

58. According to AS-17, what is a 'geographical segment'?
(A) A component engaged in providing products or services within a particular economic environment.
(B) A component engaged in providing a group of related products or services.
(C) Any part of an enterprise that operates in a different country.
(D) A reportable segment identified based on its profitability alone.

Ans :

(A) A component engaged in providing products or services within a particular economic environment.
AS-17 defines a geographical segment as a distinguishable component of an enterprise that provides products or services within a specific economic environment. This component is subject to risks and returns that are different from those of components operating in other economic environments. This helps users understand the impact of different regional factors on the enterprise.

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Oct/Nov 2022

59. According to the disclosure requirements for a primary reportable segment under AS-17, which of the following is required to be disclosed?
(A) The number of employees in the segment.
(B) The market share of the segment's products.
(C) The total carrying amount of segment assets.
(D) The names of the segment's key managers.

Ans :

(C) The total carrying amount of segment assets.
AS-17 on segment disclosures explicitly lists several required items for a primary segment. These include segment revenue, segment result, total carrying amount of segment assets, and total amount of segment liabilities, among others. The number of employees, market share, and manager names are not listed as mandatory disclosures under this specific rule.

May/June 2013

60. Under AS-18, when is the disclosure of a related party relationship required even if there have been no transactions between the parties?
(A) When a relationship of control exists between the parties.
(B) Only when both parties are public limited companies.
(C) In all circumstances, regardless of the nature of the relationship.
(D) Disclosure is never required in the absence of transactions.

Ans :

(A) When a relationship of control exists between the parties.
AS-18 makes a crucial distinction based on control. It states that the name of the related party and the nature of the relationship must be disclosed where control exists (e.g., between

a parent and its subsidiary), irrespective of whether any transactions have occurred during the period. This is because the mere existence of control can influence policies.

Oct/Nov 2018

61. As defined in AS-19, what is a 'lease'?

(A) An agreement to sell an asset at a future date for a series of payments.
(B) A contract for services that involves the use of an asset.
(C) A short-term rental agreement for natural resources like oil and gas.
(D) An agreement where the lessor conveys to the lessee the right to use an asset for an agreed period for a payment.

Ans :

(D) An agreement where the lessor conveys to the lessee the right to use an asset for an agreed period for a payment.
AS-19 defines a lease as a specific type of agreement. In this agreement, one party, the lessor, transfers the right to use an asset to another party, the lessee. This right is granted for an agreed-upon period of time in exchange for a single payment or a series of payments, without transferring the legal ownership of the asset.

May/June 2007

62. Which of the following agreements is covered under the scope of AS-19, Leases?

(A) Lease agreements to explore for natural resources.
(B) An agreement for a company to use a specific office building for five years in return for monthly payments.
(C) Licensing agreements for films and patents.
(D) A contract for courier services that does not transfer the right to use a specific vehicle.

Ans :

(B) An agreement for a company to use a specific office building for five years in return for monthly payments.
AS-19 explicitly does not apply to lease agreements for natural resources, licensing agreements for items like patents and films, or service contracts that don't transfer the right to use an asset. An agreement to use a specific building for a set period in exchange for payments fits the definition of a lease and falls within the scope of AS-19.

Oct/Nov 2025

63. What is the primary objective of AS-20, Earnings Per Share?

(A) To prescribe the minimum dividend an enterprise must pay per share.
(B) To calculate the market value of an enterprise's equity shares.
(C) To prescribe principles for determining and presenting EPS to improve performance comparison among enterprises.
(D) To mandate the presentation of EPS only for profitable enterprises.

Ans :

(C) To prescribe principles for determining and presenting EPS to improve performance comparison among enterprises.
The main objective of AS-20 is to standardize the calculation and presentation of Earnings Per Share (EPS). By establishing uniform principles, the standard aims to enhance the comparability of performance among different enterprises for a given period and also for the same enterprise over different periods. It even requires presentation if the EPS is negative.

May/June 2014

64. According to AS-21 (Revised 2016), how should the financial statements of a parent and its subsidiaries be combined to prepare consolidated financial statements?

(A) By presenting the subsidiary's statements in the notes to the parent's statements.
(B) By showing the investment in the subsidiary at cost in the parent's balance sheet.
(C) By aggregating only the profit and loss accounts of the parent and subsidiaries.
(D) On a line-by-line basis, by adding together like items of assets, liabilities, incomes, and expenses.

Ans :

(D) On a line-by-line basis, by adding together like items of assets, liabilities, incomes, and expenses.
AS-21 prescribes the line-by-line consolidation method. This involves combining the financial statements of the parent and its subsidiaries as if they were a single economic entity. This is achieved by adding together similar items of assets (like cash, inventory, PPE), liabilities,

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income, and expenses, after making necessary consolidation adjustments.

Oct/Nov 2014

65. In the context of AS-22, what are 'timing differences'?

(A) Differences between accounting income and taxable income that originate in one period and are capable of reversal in subsequent periods.

(B) Differences between accounting income and taxable income that originate in one period and never reverse.

(C) Differences between current tax and deferred tax.

(D) The time lag between earning income and paying tax on it.

Ans :

(A) Differences between accounting income and taxable income that originate in one period and are capable of reversal in subsequent periods.

AS-22 defines timing differences as those that arise because the period in which certain items are recognised for accounting purposes (accounting income) is different from the period in which they are recognised for tax purposes (taxable income). These differences originate in one period and are capable of reversing in one or more future periods.

May/June 2021

66. An investor holds 25% of the voting power of an investee company. The investor participates in the investee's policy-making processes but does not have control. As per AS-23, the investee company is classified as:

(A) A subsidiary.

(B) An associate.

(C) A joint venture.

(D) A related party with no specific classification.

Ans :

(B) An associate.

AS-23 defines an associate as an enterprise in which the investor has significant influence but not control. Significant influence is presumed to exist if the investor holds 20% or more of the voting power. Since the investor holds 25% and participates in policy-making, the investee qualifies as an associate, not a subsidiary (which requires control).

Oct/Nov 2010

67. What is the main purpose of the disclosures required by AS-24, Discontinuing Operations?

(A) To help users project future cash flows by segregating information about discontinuing operations from continuing operations.

(B) To penalise companies that decide to shut down unprofitable business segments.

(C) To combine the results of discontinuing and continuing operations to show a single profitability figure.

(D) To report only the assets of the discontinuing operation, not its profits or losses.

Ans :

(A) To help users project future cash flows by segregating information about discontinuing operations from continuing operations.

AS-24 aims to provide users of financial statements with clear and distinct information about a part of the business that is being discontinued. By segregating the financial results and cash flows of the discontinuing operation, users can make more reliable projections about the future earning capacity and financial position of the enterprise's remaining, continuing operations.

May/June 2018

68. Which of the following statements about interim financial reporting under AS-25 is correct?

(A) Measurements for interim reporting purposes should be made on a year-to-date basis.

(B) An enterprise must use different accounting policies for its interim reports than for its annual statements.

(C) Interim financial reports must always contain a complete set of financial statements, not condensed ones.

(D) Revenues received seasonally should be anticipated and recognised evenly throughout the financial year.

Ans :

(A) Measurements for interim reporting purposes should be made on a year-to-date basis.

AS-25 states that to ensure the interim report is a reliable part of the annual results, measurements for interim purposes should be made on a year-to-date basis. It also mandates using the same accounting policies as the annual statements and prohibits the anticipation or deferral of seasonal

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revenues that would not be appropriate at year-end.

Oct/Nov 2016

69. According to AS-26, which of the following is NOT a defining characteristic of an intangible asset?
(A) It is identifiable.
(B) It is a non-monetary asset.
(C) It has physical substance.
(D) It is held for use in production, supply, or for administrative purposes.

Ans :

(C) It has physical substance.
AS-26 defines an intangible asset as an identifiable non-monetary asset without physical substance. The lack of physical substance is a key characteristic that distinguishes intangible assets like patents, copyrights, and trademarks from tangible assets like property, plant, and equipment, which are covered by AS-10. The other options are part of its definition.

May/June 2024

70. Under AS-27, what is the defining feature of 'joint control'?
(A) The contractually agreed sharing of control, where decisions require the unanimous consent of the parties sharing control.
(B) One party has the power to govern the financial and operating policies of the venture.
(C) A single venturer holds more than 50% of the voting power.
(D) An investor has significant influence but not control over the economic activity.

Ans :

(A) The contractually agreed sharing of control, where decisions require the unanimous consent of the parties sharing control.
AS-27 defines joint control as the contractually agreed sharing of control over an economic activity. A critical aspect of this definition is that for key strategic, financial, and operating decisions, unanimous consent is required from the parties (venturers) who are sharing control. No single party can control the activity on its own.

Oct/Nov 2007

71. What is the primary objective of AS-28, Impairment of Assets?
(A) To prescribe the depreciation methods for all enterprise assets.
(B) To mandate the revaluation of all assets to fair value each year.
(C) To account for the disposal of assets and the resulting gains or losses.
(D) To ensure that an asset's carrying amount does not exceed its recoverable amount.

Ans :

(D) To ensure that an asset's carrying amount does not exceed its recoverable amount.
The core objective of AS-28 is to prescribe procedures to ensure that an enterprise's assets are not carried at more than their recoverable amount. An asset is considered impaired if its carrying amount (book value) is greater than the amount expected to be recovered through its use or sale, and the standard requires recognition of an impairment loss.

May/June 2009

72. As per AS-28, the 'recoverable amount' of an asset is the:
(A) Original cost of the asset less accumulated depreciation.
(B) Higher of the asset's net selling price and its value in use.
(C) Lower of the asset's net selling price and its value in use.
(D) Present value of all future cash flows from the asset.

Ans :

(B) Higher of the asset's net selling price and its value in use.
AS-28 defines the recoverable amount as the higher of two values: the asset's net selling price (the amount obtainable from sale in an arm's length transaction, less disposal costs) and its 'value in use' (the present value of future cash flows expected from its continuing use and ultimate disposal). An impairment loss is recognized if the carrying amount exceeds this recoverable amount.

Oct/Nov 2019

73. Under AS-29 (Revised 2016), a provision should be recognised only when three specific conditions

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are met. Which of the following is NOT one of those conditions?

(A) The enterprise has a present obligation as a result of a past event.
(B) It is probable that an outflow of resources will be required to settle the obligation.
(C) The obligation has been legally enforced through a court order.
(D) A reliable estimate can be made of the amount of the obligation.

Ans :

(C) The obligation has been legally enforced through a court order.

AS-29 requires recognition of a provision when there is a present obligation from a past event, a probable outflow of resources, and a reliable estimate of the amount. The present obligation can be legal or constructive; it does not have to be formally enforced by a court at the time of recognition to warrant making a provision.

May/June 2010

74. How does AS-29 require an enterprise to treat a contingent liability?

(A) Recognise it as a liability on the balance sheet.
(B) Recognise it as a liability only if the amount can be estimated with 100% certainty.
(C) Do not recognise or disclose it under any circumstances.
(D) Do not recognise it, but disclose it in the notes unless the possibility of an outflow is remote.

Ans :

(D) Do not recognise it, but disclose it in the notes unless the possibility of an outflow is remote.

AS-29 strictly prohibits the recognition of a contingent liability in the balance sheet because it is either a possible obligation or a present obligation that does not meet the recognition criteria (not probable or not reliably measurable). Instead, it requires disclosure of the contingent liability in the notes to the financial statements, unless the possibility of an outflow is remote.

Oct/Nov 2013

75. What is the primary motivation for introducing Indian Accounting Standards (Ind AS)?

(A) To make Indian financial statements uniform and comparable with those of global companies by converging with IFRS.
(B) To create a set of accounting standards unique to India with no global parallels.
(C) To reduce the number of accounting standards applicable to Indian companies.
(D) To completely replace the Companies Act, 2013, with new accounting rules.

Ans :

(A) To make Indian financial statements uniform and comparable with those of global companies by converging with IFRS.

The main reason for introducing Ind AS was to align India's accounting framework with global standards. Ind AS are a converged form of International Financial Reporting Standards (IFRS). This convergence aims to make the financial statements of Indian companies more uniform, transparent, and easily comparable for global investors, thus enhancing access to international capital markets.

May/June 2020

76. As per the Companies (Indian Accounting Standards) Rules, 2015, which of the following unlisted companies is required to follow Ind AS based on its net worth?

(A) An unlisted company with a net worth of ₹150 crore.
(B) An unlisted company with a net worth of ₹275 crore.
(C) An unlisted company with a net worth of ₹200 crore.
(D) An unlisted company with a net worth of ₹240 crore.

Ans :

(B) An unlisted company with a net worth of ₹275 crore.

The rules specify a clear threshold for the mandatory adoption of Ind AS by unlisted companies. Unlisted companies with a net worth of ₹250 crore or more are required to comply. Among the given options, only the company with a net worth of ₹275 crore meets and exceeds this specified threshold.

Oct/Nov 2005

77. As per the RBI circular dated March 22, 2019, what is the current status of Ind AS implementation for scheduled commercial banks?

(A) It was made mandatory from April 1, 2018.
(B) It was deferred by one year to April 1, 2019.
(C) It has been made voluntary for all banks.

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(D) It has been deferred till further notice.

Ans :

(D) It has been deferred till further notice.
The RBI, through its circular dated March 22, 2019, deferred the implementation of Ind AS for banks. This deferral was due to the need for legislative amendments to the Banking Regulation Act, 1949, and other factors. The implementation remains postponed 'till further notice', with no new mandatory date set at that time.

May/June 2017

78. The impairment requirements of Ind AS 109 are based on which model, replacing the previous incurred loss model?
(A) Expected Credit Loss (ECL) model.
(B) Historical Cost Loss (HCL) model.
(C) Fair Value Loss (FVL) model.
(D) Realisable Value Loss (RVL) model.

Ans :

(A) Expected Credit Loss (ECL) model.
A significant change introduced by Ind AS 109 is the shift in the impairment methodology for financial assets. It replaces the 'incurred loss' model (where losses are recognised only after a loss event has occurred) with a forward-looking 'Expected Credit Loss' (ECL) model. This new model requires banks to provision for expected losses from the time a loan is originated.

Oct/Nov 2020

79. A bank has a portfolio of loans where there has not been a significant increase in credit risk since they were first given. Under the three-stage approach of Ind AS 109, what level of Expected Credit Loss (ECL) must the bank recognise for these exposures?
(A) Lifetime ECL - Credit Impaired.
(B) Lifetime ECL - Not Credit Impaired.
(C) 12-Months ECL.
(D) No ECL needs to be recognised.

Ans :

(C) 12-Months ECL.
The three-stage model in Ind AS 109 categorizes financial assets based on their credit quality. For exposures in Stage 1, where there has been no significant increase in credit risk since initial recognition, the bank is required to recognise a 12-Months ECL. This represents the portion of lifetime ECL associated with default events possible within the next twelve months.

May/June 2006

80. Match the Ind AS number from List-I with its corresponding standard name from List-II.
List-I (Ind AS No.)
P. Ind AS 101
Q. Ind AS 113
R. Ind AS 116
S. Ind AS 16
List-II (Standard Name)
1. Leases
2. Property, Plant and Equipment
3. First-time Adoption of Indian Accounting Standards
4. Fair Value Measurement
(A) P-3, Q-4, R-1, S-2
(B) P-2, Q-1, R-4, S-3
(C) P-3, Q-2, R-1, S-4
(D) P-4, Q-3, R-2, S-1

Ans :

(A) P-3, Q-4, R-1, S-2
According to the list of Indian Accounting Standards, Ind AS 101 relates to the First-time Adoption of Indian Accounting Standards. Ind AS 113 is for Fair Value Measurement. Ind AS 116 deals with Leases, and Ind AS 16 covers Property, Plant and Equipment. The correct matching is therefore P-3, Q-4, R-1, and S-2.

Oct/Nov 2008

81. Which Ind AS provides standards for 'Provisions, Contingent Liabilities and Contingent Assets'?
(A) Ind AS 36
(B) Ind AS 38
(C) Ind AS 40
(D) Ind AS 37

Ans :

(D) Ind AS 37
As per standard lists of Ind AS, Ind AS 37 is titled 'Provisions, Contingent Liabilities and Contingent Assets'. This standard provides the criteria for recognition, measurement, and disclosure for these items, and is converged with the corresponding international standard. Ind AS 36 deals with Impairment, Ind AS 38 with Intangible Assets, and Ind AS 40 with Investment Property.

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May/June 2015

82. What is the main purpose of US GAAP?
(A) To ensure that all companies are profitable.
(B) To bring transparency and consistency in financial reporting among various organisations.
(C) To provide accounting rules for use only by government entities in the USA.
(D) To provide definite assurance that a company's financial statements are free from all errors.

Ans :

(B) To bring transparency and consistency in financial reporting among various organisations.
The primary purpose of Generally Accepted Accounting Principles (US GAAP) is to establish a common set of rules and standards for financial reporting. This framework aims to ensure that the financial statements prepared by different companies are consistent and transparent, allowing users to make meaningful comparisons and informed decisions. It does not, however, guarantee error-free statements.

Oct/Nov 2023

83. In the United States, which body currently sets the accounting principles for the profession (for non-governmental entities)?
(A) United States Securities and Exchange Commission (SEC).
(B) American Institute of Certified Public Accountants (AICPA).
(C) Financial Accounting Standards Board (FASB).
(D) Governmental Accounting Standards Board (GASB).

Ans :

(C) Financial Accounting Standards Board (FASB).
While the SEC has the authority, it has historically encouraged the private sector to set accounting standards. The Financial Accounting Standards Board (FASB) is the primary private-sector body responsible for establishing and improving Generally Accepted Accounting Principles (GAAP) for non-governmental entities in the United States. The GASB sets standards for state and local governments.

May/June 2022

84. According to the fundamental qualities of financial statements under US GAAP, what does the quality of 'Reliability' imply?
(A) The information is available on time before decisions are made.
(B) The information makes a difference in a decision.
(C) The information is reported in a similar manner for different enterprises.
(D) The information is verifiable, neutral, and has representational faithfulness.

Ans :

(D) The information is verifiable, neutral, and has representational faithfulness.
The quality of 'Reliability' under US GAAP means that the information can be trusted by users. This is achieved when the information is verifiable (independent parties would reach similar conclusions), neutral (free from bias), and possesses representational faithfulness (it reflects the economic reality of what it purports to represent).

Oct/Nov 2015

85. In the GAAP hierarchy, which of the following is placed in the most authoritative level of GAAP?
(A) FASB Standards and Interpretations.
(B) FASB Technical Bulletins.
(C) AICPA Industry Audit and Accounting Guides.
(D) FASB Emerging Issues Task Force (EITF).

Ans :

(A) FASB Standards and Interpretations.
The 'House of GAAP' illustrates the hierarchy of accounting literature. The top category represents the most authoritative level. This top-tier category includes FASB Standards and Interpretations and APB Opinions. The other options, such as Technical Bulletins, EITF pronouncements, and AICPA Guides, are placed in lower, less authoritative categories.

May/June 2008

86. The International Accounting Standards (IAS) were issued between 1973 and 2001 by which body?
(A) International Accounting Standards Board (IASB).
(B) International Accounting Standards Committee (IASC).

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(C) Financial Accounting Standards Board (FASB).
(D) IFRS Foundation.

Ans :

(B) International Accounting Standards Committee (IASC).
The original set of global standards, known as International Accounting Standards (IAS), were developed and issued by the Board of the International Accounting Standards Committee (IASC) from 1973 until 2001. In 2001, the IASC was succeeded by the new International Accounting Standards Board (IASB), which continues to develop standards, now called IFRS.

Oct/Nov 2024

87. Which of the following is a principal objective of the IFRS Foundation?
(A) To develop separate accounting standards for each country.
(B) To audit companies to ensure they are applying IFRS correctly.
(C) To set accounting standards only for small and medium-sized entities (SMEs).
(D) To develop a single set of high-quality, understandable, and globally accepted IFRSs.

Ans :

(D) To develop a single set of high-quality, understandable, and globally accepted IFRSs.
A principal objective of the IFRS Foundation is to develop a single set of high-quality, understandable, enforceable, and globally accepted International Financial Reporting Standards (IFRSs). This is done through its standard-setting body, the IASB. The goal is to create a common language for business affairs across international boundaries.

May/June 2019

88. What is the role of the IFRS Interpretations Committee (IFRIC)?
(A) To review widespread accounting issues within current IFRSs and provide authoritative guidance.
(B) To develop new IFRS standards from scratch.
(C) To enforce the application of IFRS in non-compliant countries.
(D) To fund the activities of the IFRS Foundation and the IASB.

Ans :

(A) To review widespread accounting issues within current IFRSs and provide authoritative guidance.
The IFRS Interpretations Committee (formerly IFRIC) is the interpretative body of the IASB. Its mandate is to address, on a timely basis, widespread and practical accounting issues that arise within the context of existing International Financial Reporting Standards. It provides authoritative guidance on these issues to ensure consistent application of the standards globally.

NODIA

Oct/Nov 2011

89. A key difference between US GAAP and IFRS is that US GAAP is generally considered more _____, while IFRS is more _____.
(A) principles-based; rules-based
(B) recent; outdated
(C) rules-based; principles-based
(D) complex; simple

Ans :

(C) rules-based; principles-based
A fundamental philosophical difference exists between the two frameworks. US GAAP is often described as being more 'rules-based', providing detailed and specific rules for a wide variety of situations. In contrast, IFRS is considered more 'principles-based', setting out broader principles and requiring more professional judgment in applying them to specific transactions.

May/June 2025

90. How is the valuation of fixed assets treated differently under US GAAP and IFRS?
(A) IFRS allows both cost and revaluation models, while GAAP primarily uses the cost model.
(B) GAAP allows both cost and revaluation models, while IFRS only allows the cost model.
(C) Both GAAP and IFRS exclusively use the historical cost model for fixed assets.
(D) Both GAAP and IFRS exclusively use the revaluation model for fixed assets.

Ans :

(A) IFRS allows both cost and revaluation models, while GAAP primarily uses the cost model.
Under US GAAP, fixed assets are valued using the cost model (historical cost less accumulated depreciation). In contrast, IFRS provides an alternative. While the cost model is permitted,

IFRS also allows the use of the revaluation model, where assets are carried at a revalued amount based on fair value.

Oct/Nov 2006

91. Which inventory valuation method is permitted under US GAAP but not under IFRS?
(A) FIFO (First-In, First-Out).
(B) Weighted-average cost.
(C) Specific identification.
(D) LIFO (Last-In, First-Out).

Ans :

(D) LIFO (Last-In, First-Out).
Comparisons of the two frameworks show that US GAAP allows the use of LIFO, FIFO, or weighted-average cost methods. In contrast, IFRS permits only the FIFO or weighted-average cost methods and explicitly does not permit the use of LIFO.

May/June 2012

92. What does 'Transfer Pricing' refer to?
(A) The price at which goods are sold to the final external customer.
(B) The pricing of goods and services transacted between different divisions of a multi-entity company.
(C) The additional cost added to products to cover transportation expenses.
(D) The process of adjusting prices to account for inflation.

Ans :

(B) The pricing of goods and services transacted between different divisions of a multi-entity company.
Transfer pricing is the concept of setting a price for goods and services that are exchanged between related entities within a larger organization, such as between a parent company and a subsidiary, or between two divisions. This price affects how profits are allocated among the different parts of the company, which has significant tax implications.

Oct/Nov 2017

93. What is the 'arm's length principle' in the context of transfer pricing?
(A) The price should be set to maximize profit in the division with the lowest tax rate.
(B) The price is determined by adding a fixed 10% markup to the cost of production.
(C) The price should be what two unrelated and non-desperate parties would agree to in a transaction.
(D) The price is dictated by the government of the country where the transaction occurs.

Ans :

(C) The price should be what two unrelated and non-desperate parties would agree to in a transaction.
The arm's length principle is the international standard for determining transfer prices for tax purposes. It dictates that the price for a transaction between related parties should be the same as the price that would have been agreed upon if the parties were independent and unrelated, conducting the transaction under similar conditions.

May/June 2005

94. Which traditional transfer pricing method compares the price of a controlled transaction to the price of a comparable uncontrolled transaction?
(A) Cost Plus Method.
(B) Resale Price Method.
(C) Transactional Net Margin Method (TNMM).
(D) Comparable Uncontrolled Price (CUP) Method.

Ans :

(D) Comparable Uncontrolled Price (CUP) Method.
The Comparable Uncontrolled Price (CUP) method is considered the most direct way to apply the arm's length principle. It determines the arm's length price by directly comparing the price charged for property or services transferred in a controlled transaction (between related parties) to the price charged in a comparable uncontrolled transaction (between unrelated parties).

Oct/Nov 2012

95. A manufacturing division incurs costs of ₹500 (materials, labour, etc.) to produce a finished good. It sells this good to its related distribution division. To determine the transfer price, an appropriate mark-up is added, based on the profits of comparable independent companies. Which transfer pricing method is being used?
(A) Cost Plus Method.
(B) Resale Price Method.

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(C) Comparable Uncontrolled Price Method.
(D) Profit Split Method.

Ans :

(A) Cost Plus Method.
The Cost Plus (CP) method determines the arm's length price by starting with the costs incurred by the supplier in the controlled transaction. An appropriate gross profit mark-up is then added to these costs. The mark-up is determined by reference to the mark-ups earned by comparable independent companies. This scenario perfectly describes the CP method.

May/June 2016

96. Which non-traditional transfer pricing method is typically applied when businesses are too integrated for separate evaluation, and it involves splitting the ultimate profit based on the level of contribution from each party?
(A) Transactional Net Margin Method (TNMM).
(B) Profit Split (PS) Method.
(C) Resale Price Method.
(D) Cost Plus Method.

Ans :

(B) Profit Split (PS) Method.
The Profit Split (PS) method is used for highly integrated operations where it's difficult to evaluate transactions on a standalone basis. Instead of pricing individual transactions, this method identifies the total profit from the combined endeavor and then splits it between the related parties based on their relative contributions, functions performed, and risks assumed.

Oct/Nov 2021

97. In the context of banking, what is the Transfer Price Mechanism (TPM) generally used for?
(A) To set the interest rate for customer loans.
(B) To determine the fees for credit card services.
(C) To calculate the exchange rate for foreign currency transactions with customers.
(D) To evaluate the performance of branches by charging interest on funds transferred between them.

Ans :

(D) To evaluate the performance of branches by charging interest on funds transferred between them.
Within a bank, the Transfer Price Mechanism (TPM) is used as an internal tool, primarily for performance evaluation. The transfer price is the interest rate charged by a branch with surplus funds to a branch with a deficit of funds. This mechanism helps in assessing the profitability of each branch as a separate unit.

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May/June 2023

98. How many mandatory and non-mandatory standards has the ICAI issued so far?
(A) Twenty-nine mandatory and three non-mandatory standards.
(B) Twenty-five mandatory and five non-mandatory standards.
(C) Thirty-two mandatory and zero non-mandatory standards.
(D) Twenty-three mandatory and nine non-mandatory standards.

Ans :

(A) Twenty-nine mandatory and three non-mandatory standards.
A summary of the ICAI's activities indicates that "The Institute of Chartered Accountants of India (ICAI) has so far issued twenty-nine mandatory and three non-mandatory standards." This is a factual statement about the number of standards issued.

Oct/Nov 2009

99. What is the primary objective of Ind AS 101, First-time Adoption of Indian Accounting Standards?
(A) To provide an exemption from applying any Ind AS in the first year.
(B) To require the retrospective application of all Ind AS standards without any exceptions.
(C) To ensure an entity's first Ind AS financial statements contain high-quality information and provide a suitable starting point.
(D) To detail the differences between Ind AS and previous Indian GAAP.

Ans :

(C) To ensure an entity's first Ind AS financial statements contain high-quality information and provide a suitable starting point.
Ind AS 101 is designed to manage the transition to Ind AS. Its objective is to ensure that an entity's first Ind AS financial statements, and its interim reports for that period, are transparent, comparable, and provide a suitable starting point

for future accounting under Ind AS, while also ensuring the costs do not exceed the benefits.

May/June 2011

100. Under Ind AS 102, Share-based Payment, if goods or services are received in an equity-settled share-based payment transaction, the entity shall recognise a corresponding increase in:
(A) equity.
(B) a liability.
(C) revenue.
(D) cash.

Ans :

(A) equity.
Ind AS 102 specifies the accounting treatment based on how the transaction is settled. For an equity-settled transaction, where the entity issues its own equity instruments (like shares or options) in exchange for goods or services, it recognizes the received goods/services as an asset or expense, with a corresponding increase directly in equity.

Oct/Nov 2022

101. Ind AS 103, Business Combinations, does NOT apply to which of the following?
(A) The acquisition of a subsidiary that constitutes a business.
(B) The measurement of goodwill acquired in a business combination.
(C) The recognition of identifiable assets acquired in a business combination.
(D) The accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself.

Ans :

(D) The accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself.
Ind AS 103 establishes the principles for accounting for business combinations, where an acquirer obtains control of a business. It explicitly states that the standard does not apply to the formation of a joint arrangement in the financial statements of the joint arrangement itself. Such arrangements are covered by other standards like Ind AS 111.

May/June 2013

102. A key requirement of Ind AS 105, Non-current Assets Held for Sale and Discontinued Operations, is that assets classified as held for sale should be:
(A) measured at the higher of carrying amount and fair value less costs to sell.
(B) measured at the lower of carrying amount and fair value less costs to sell, and depreciation should cease.
(C) depreciated at an accelerated rate until they are sold.
(D) presented combined with other current assets in the balance sheet.

Ans :

(B) measured at the lower of carrying amount and fair value less costs to sell, and depreciation should cease.
Ind AS 105 has specific measurement and presentation rules. Once a non-current asset is classified as 'held for sale', its depreciation is stopped. It is then measured at the lower of its current carrying amount and its fair value less the costs to sell it. This ensures the asset is not valued at more than its net recoverable amount.

Oct/Nov 2018

103. Under Ind AS 109, Financial Instruments, when should an entity derecognise a financial asset?
(A) When the fair value of the asset falls below its carrying amount.
(B) When the entity changes its business model for managing the asset.
(C) When the contractual rights to the cash flows from the financial asset expire.
(D) When the entity decides to classify the asset as held-to-maturity.

Ans :

(C) When the contractual rights to the cash flows from the financial asset expire.
Ind AS 109 provides clear criteria for derecognition (removal from the balance sheet). An entity must derecognise a financial asset when its rights to receive cash flows from that asset have expired (e.g., a loan is fully repaid). It also derecognises the asset if it transfers the asset and substantially all the risks and rewards of ownership.

May/June 2007

104. According to Ind AS 110, an investor controls an investee if and only if the investor has all of the following EXCEPT:

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(A) Power over the investee.
(B) Exposure, or rights, to variable returns from its involvement with the investee.
(C) The ability to use its power over the investee to affect the amount of the investor's returns.
(D) Legal ownership of more than 50% of the investee's shares.

Ans :

(D) Legal ownership of more than 50% of the investee's shares.
Ind AS 110 defines control based on three essential elements: power, exposure to variable returns, and the ability to use that power to affect those returns. While owning more than 50% of shares often leads to control, it is not a mandatory element in itself. Control can exist even without majority ownership, for example, through contractual arrangements.

Oct/Nov 2025

105. Under Ind AS 111, what is the key difference between a 'joint operation' and a 'joint venture'?
(A) In a joint operation parties have rights to assets and obligations for liabilities; in a joint venture, parties have rights to the net assets.
(B) A joint operation involves two parties, while a joint venture involves three or more.
(C) Joint operations are accounted for using the equity method, while joint ventures use proportionate consolidation.
(D) A joint operation is for short-term projects, while a joint venture is for long-term arrangements.

Ans :

(A) In a joint operation parties have rights to assets and obligations for liabilities; in a joint venture, parties have rights to the net assets.
Ind AS 111 classifies joint arrangements based on the rights and obligations of the parties. In a joint operation, the parties (joint operators) have direct rights to the assets and obligations for the liabilities of the arrangement. In a joint venture, the parties (joint venturers) have rights only to the net assets of the arrangement.

May/June 2014

106. How does Ind AS 113 define 'fair value'?
(A) The price that was paid to acquire an asset or received to assume a liability.
(B) The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants.
(C) The value of an asset based on its usefulness to the specific entity holding it.
(D) The recoverable amount of an asset, which is the higher of its value in use and net selling price.

Ans :

(B) The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants.
Ind AS 113 provides a precise, market-based definition of fair value. It is an exit price – the price that would be received from selling an asset or paid to transfer a liability. The definition emphasizes that this is in an 'orderly transaction' (not a forced sale) between 'market participants' (knowledgeable, willing parties) at the measurement date.

Oct/Nov 2014

107. What is the core principle of Ind AS 115, Revenue from Contracts with Customers?
(A) Recognise revenue when cash is received from the customer.
(B) Recognise revenue on a straight-line basis over the life of the contract.
(C) Recognise revenue only when the contract is fully completed and all services have been rendered.
(D) Recognise revenue to depict the transfer of promised goods or services in an amount that reflects the consideration the entity expects to be entitled to.

Ans :

(D) Recognise revenue to depict the transfer of promised goods or services in an amount that reflects the consideration the entity expects to be entitled to.
The core principle of Ind AS 115 is centered on the transfer of control. An entity recognizes revenue when (or as) it satisfies a performance obligation by transferring a promised good or service to a customer. The amount recognized reflects the consideration the entity expects to receive in exchange for those goods or services.

May/June 2021

108. A significant change introduced by Ind AS 116, Leases, is that for most lease contracts, lessees have to:
(A) recognise a 'right-of-use asset' and a

NODIA

corresponding lease liability on the balance sheet.
(B) recognise lease payments as an operating expense on a straight-line basis.
(C) classify all leases as either finance or operating leases.
(D) disclose lease commitments only in the notes to the financial statements.

Ans :

(A) recognise a 'right-of-use asset' and a corresponding lease liability on the balance sheet.
Ind AS 116 fundamentally changed lease accounting for lessees. It eliminated the distinction between finance and operating leases for lessees. For most leases, the lessee is now required to bring the lease onto the balance sheet by recognizing a 'right-of-use asset' (representing its right to use the underlying asset) and a 'lease liability' (representing its obligation to make lease payments).

Oct/Nov 2010

109. According to Ind AS 1, which of the following is part of a complete set of financial statements?
(A) A statement of management's objectives for the next period.
(B) A detailed report on corporate social responsibility activities.
(C) A statement of changes in equity for the period.
(D) A report on the company's market share and competitive position.

Ans :

(C) A statement of changes in equity for the period.
Ind AS 1 explicitly lists the components of a complete set of financial statements. Among the items listed are the balance sheet, statement of profit and loss, statement of cash flows, notes, and the statement of changes in equity for the period. The other options are not part of this required set.

May/June 2018

110. Under Ind AS 1, when is an entity required to prepare its financial statements on a basis other than the 'going concern' basis?
(A) When management intends to liquidate the entity or cease trading, or has no realistic alternative.
(B) When the entity has incurred a loss for two consecutive years.
(C) When the entity's debt-to-equity ratio exceeds a certain prescribed limit.
(D) When there is a significant change in the ownership of the entity.

Ans :

(A) When management intends to liquidate the entity or cease trading, or has no realistic alternative.
The going concern assumption is fundamental, but Ind AS 1 specifies when it should not be used. An entity must abandon the going concern basis if management makes a firm decision to liquidate the entity or cease its operations, or if external circumstances leave no other realistic option. In such cases, the basis of preparation must be disclosed.

Oct/Nov 2016

111. Ind AS 2 on Inventories does NOT apply to which of the following?
(A) Manufactured goods.
(B) Raw materials.
(C) Work in progress of a manufacturing entity.
(D) Biological assets related to agricultural activity.

Ans :

(D) Biological assets related to agricultural activity.
Ind AS 2 specifies its scope exclusions. The standard does not apply to biological assets (like living animals or plants) related to agricultural activity and agricultural produce at the point of harvest. These items are covered under Ind AS 41, Agriculture, which has its own specific measurement rules.

May/June 2024

112. Under Ind AS 7, a single transaction, such as the repayment of a loan including interest and principal, may result in cash flows that are:
(A) classified entirely as an operating activity.
(B) classified differently (e.g., interest as operating and principal as financing).
(C) classified entirely as a financing activity.
(D) excluded from the cash flow statement.

Ans :

(B) classified differently (e.g., interest as operating and principal as financing).

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Ind AS 7 acknowledges that a single transaction can have components belonging to different activities. For a loan repayment, the principal portion is a financing activity as it repays the original borrowing. The interest portion, however, can be classified as either an operating activity (as it relates to the cost of financing operations) or a financing activity, but the components are split.

Oct/Nov 2007

113. According to Ind AS 10, what is a 'non-adjusting event' after the reporting period?
(A) An event that provides evidence of conditions that existed at the end of the reporting period.
(B) An event that requires the restatement of the financial statements.
(C) An event that is indicative of conditions that arose after the reporting period.
(D) The discovery of a material fraud that occurred during the reporting period.

Ans :

(C) An event that is indicative of conditions that arose after the reporting period.
Ind AS 10 distinguishes between two types of events after the reporting period. A non-adjusting event is one that relates to conditions that did not exist at the balance sheet date but arose subsequently. Such events do not result in adjustments to the amounts in the financial statements but may require disclosure if they are material.

May/June 2009

114. As per Ind AS 12, what is 'Taxable income (loss)'?
(A) The profit or loss for a period before deducting tax expenses.
(B) The aggregate of current tax and deferred tax charged to the profit and loss statement.
(C) The amount attributed to an asset or liability for tax purposes.
(D) The amount of income (loss) for a period determined in accordance with tax laws.

Ans :

(D) The amount of income (loss) for a period determined in accordance with tax laws.
Ind AS 12 defines 'Taxable income (loss)' as the net profit or loss for a period, calculated according to the rules established by the tax authorities (tax laws). This is the figure upon which income tax payable is determined. It often differs from 'Accounting profit', which is calculated based on accounting standards.

Oct/Nov 2019

115. Which of the following statements is a salient feature of Ind AS 16, Property, Plant and Equipment?
(A) Each part of a PPE item with a significant cost must be depreciated separately.
(B) Depreciation is the unsystematic allocation of an asset's cost over its useful life.
(C) Useful life is the total physical life of the asset, regardless of its use by the entity.
(D) The standard applies to biological assets related to agricultural activity.

Ans :

(A) Each part of a PPE item with a significant cost must be depreciated separately.
Ind AS 16 requires a component-based approach to depreciation. If an item of Property, Plant, and Equipment (PPE) is composed of parts with different useful lives and significant costs relative to the total cost (e.g., an aircraft's engine and body), each such significant part must be depreciated separately over its own useful life.

May/June 2010

116. Under Ind AS 19, Employee Benefits, a post-employment benefit plan where an entity pays fixed contributions into a separate fund and has no legal or constructive obligation to pay further if the fund is insufficient is called a:
(A) Defined benefit plan.
(B) Defined contribution plan.
(C) Short-term employee benefit plan.
(D) Termination benefit plan.

Ans :

(B) Defined contribution plan.
Ind AS 19 classifies post-employment plans based on their economic substance. A defined contribution plan is characterized by the employer's obligation being limited to the fixed contributions they agree to pay. The investment risk and actuarial risk fall on the employee. The employer has no further obligation if the fund's assets are not sufficient.

Oct/Nov 2013

117. Ind AS 20, which deals with accounting for government grants, does NOT apply to which of the following?

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(A) Government grants in the form of subsidies.
(B) Duty drawbacks received from the government.
(C) Grants of non-monetary assets from the government.
(D) Government grants covered by Ind AS 41 (Agriculture).

Ans :

(D) Government grants covered by Ind AS 41 (Agriculture).
Ind AS 20 lists specific exclusions from its scope. It explicitly states that the standard does not deal with government grants that are covered by Ind AS 41, Agriculture. This is because Ind AS 41 has its own specific rules for accounting for government grants related to biological assets.

May/June 2020

118. According to Ind AS 21, what is 'Functional Currency'?
(A) The currency of the primary economic environment in which the entity operates.
(B) The currency used in presenting the financial statements.
(C) Any currency other than the functional currency of an enterprise.
(D) The official currency of the country where the company is legally incorporated.

Ans :

(A) The currency of the primary economic environment in which the entity operates.
Ind AS 21 defines functional currency as the currency of the primary economic environment in which an entity operates. It is the currency in which the entity primarily generates and expends cash. This is a key concept as it determines how foreign currency transactions are measured and translated, and it may be different from the presentation currency.

Oct/Nov 2005

119. An enterprise has a related party relationship with its subsidiary where it holds 80% of the shares (control exists). During the year, no transactions occurred between the parent and the subsidiary. According to Ind AS 24, what disclosure is required?
(A) No disclosure is needed as there were no transactions.
(B) Only the volume and amount of potential future transactions must be disclosed.
(C) The name of the subsidiary and the nature of the relationship (control) must be disclosed.
(D) A statement that no transactions occurred, without naming the related party.

Ans :

(C) The name of the subsidiary and the nature of the relationship (control) must be disclosed.
Ind AS 24 mandates that where a control relationship exists (like between a parent and its subsidiary), the relationship must be disclosed regardless of whether there have been any transactions. The mere existence of control can influence the policies of the subsidiary, and users of financial statements need to be aware of this.

May/June 2017

120. What is the 'equity method' of accounting as described in Ind AS 28?
(A) The investment is initially recognised at cost and subsequently adjusted for the investor's share of the investee's profit or loss.
(B) The investment is always carried at its fair value, with changes recognised in profit or loss.
(C) The investment is always carried at its original cost without any subsequent adjustments.
(D) The investor recognises its proportionate share of the investee's assets and liabilities in its own balance sheet.

Ans :

(A) The investment is initially recognised at cost and subsequently adjusted for the investor's share of the investee's profit or loss.
The equity method, used for associates and joint ventures, begins with the investment recorded at cost. In subsequent periods, the carrying amount is increased or decreased to recognise the investor's share of the investee's post-acquisition profits or losses. Dividends received from the investee are treated as a reduction of the investment's carrying amount.

Oct/Nov 2020

121. Consider the following:
Assertion (A): In a hyperinflationary economy, reporting financial results in the local currency without restatement is not useful.
Reason (R) : Money loses purchasing power at such a rapid rate that comparing amounts from different times, even within the same period, is misleading.

NODIA

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Ind AS 29 is based on the premise that in a hyperinflationary economy, money's purchasing power erodes so quickly that historical cost figures become meaningless. The assertion is true because un-restated figures are not comparable. The reason is also true and correctly explains why this is the case—the rapid loss of purchasing power makes comparisons misleading.

May/June 2006

122. According to Ind AS 32, which of the following is a 'financial asset'?
(A) A contractual obligation to deliver cash to another entity.
(B) A contractual right to receive cash or another financial asset from another enterprise.
(C) A physical asset such as inventory or property.
(D) A residual interest in the assets of an entity after deducting all its liabilities.

Ans :

(B) A contractual right to receive cash or another financial asset from another enterprise.
Ind AS 32 defines a financial asset based on the rights it confers. A key part of this definition is having a contractual right to receive cash or another financial asset (e.g., an account receivable). It also includes an equity instrument of another entity. A contractual obligation to deliver cash is a financial liability, and a residual interest is an equity instrument.

Oct/Nov 2008

123. How does Ind AS 33 require an enterprise to present basic and diluted earnings per share (EPS)?
(A) Only in the notes to the financial statements.
(B) Only if the EPS amounts are positive.
(C) On the face of the statement of profit and loss.
(D) In a separate, standalone EPS report.

Ans :

(C) On the face of the statement of profit and loss.
Ind AS 33 mandates prominent presentation of earnings per share. It requires an enterprise to present both basic and diluted EPS directly on the face of the statement of profit and loss (and other comprehensive income) for each class of ordinary shares. This requirement holds even if the resulting EPS amounts are negative (i.e., a loss per share).

May/June 2015

124. Based on Ind AS 38, which of the following is classified as a Capital Expenditure?
(A) Costs of day-to-day servicing of assets.
(B) Costs of major inspections for potential faults in assets.
(C) Costs of opening a new facility.
(D) Administrative and other general costs.

Ans :

(B) Costs of major inspections for potential faults in assets.
Ind AS 38 and related standards categorize costs. 'Subsequent costs' that are classified as Capital Expenditure include costs of parts requiring replacement at regular intervals and costs of major inspections for potential faults. In contrast, costs of day-to-day servicing, opening a new facility, and general administrative costs are typically treated as revenue expenditure.

Oct/Nov 2023

125. According to Ind AS 40, property held to earn rentals or for capital appreciation, rather than for use in production or for sale in the ordinary course of business, is known as:
(A) Owner-occupied property.
(B) Property, plant, and equipment.
(C) Investment property.
(D) Intangible property.

Ans :

(C) Investment property.
Ind AS 40 provides a specific definition for 'Investment property'. The key criterion is the purpose for which the property (land or a building) is held. If it is held to generate rental income or for capital appreciation (or both), it is classified as investment property. This distinguishes it from owner-occupied property used in operations.

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May/June 2022

126. An entity owns a building. It uses 70% of the building for its own administrative purposes and leases out the remaining 30 % to an independent third party under an operating lease. How would this building be treated under Ind AS 40 and Ind AS 16?

(A) The entire building is treated as Investment Property under Ind AS 40.
(B) The entire building is treated as Owner-Occupied Property under Ind AS 16.
(C) The building is classified as inventory.
(D) The 70% portion is Owner-Occupied Property (Ind AS 16) and the 30 % portion is Investment Property (Ind AS 40), if they can be sold separately.

Ans :

(D) The 70% portion is Owner-Occupied Property (Ind AS 16) and the 30 % portion is Investment Property (Ind AS 40), if they can be sold separately.
When a property has portions used for different purposes, the accounting treatment depends on whether the portions can be separated. If the parts can be sold or leased out separately, the owner-occupied portion is accounted for under Ind AS 16 (PPE), and the portion held to earn rentals is accounted for as Investment Property under Ind AS 40.

Oct/Nov 2015

127. Under Ind AS 41, Agriculture, when should an entity recognise a biological asset or agricultural produce?

(A) When the entity controls the asset, future economic benefits are probable, and fair value or cost can be measured reliably.
(B) Only when the asset has been physically sold.
(C) As soon as the entity decides to engage in agricultural activity.
(D) Only when the asset reaches maturity and is ready for harvest.

Ans :

(A) When the entity controls the asset, future economic benefits are probable, and fair value or cost can be measured reliably.
Ind AS 41 sets out three specific criteria for the recognition of a biological asset or agricultural produce. All three conditions must be met: the entity must control the asset as a result of past events; it must be probable that future economic benefits will flow to the entity; and the fair value or cost can be measured reliably.

May/June 2008

128. How should agricultural produce harvested from an entity's biological assets be measured at the point of harvest, according to Ind AS 41?

(A) At its historical cost of production.
(B) At its fair value less costs to sell.
(C) At its net realisable value.
(D) At zero value until it is sold.

Ans :

(B) At its fair value less costs to sell.
Ind AS 41 mandates a specific measurement basis for agricultural produce at the point of harvest. It must be measured at its fair value less the estimated costs to sell it. This measurement at the point of harvest then becomes the initial 'cost' for the purpose of applying Ind AS 2 (Inventories) if the produce is held for sale.

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Oct/Nov 2024

129. Consider the following statements regarding accounting principles:

1. Stewardship accounting is a modern concept that emerged with the knowledge economy.
2. Cost accounting developed in response to the needs of the Industrial Revolution.
3. Management accounting is forward-looking and largely free from the constraints of accounting standards.
4. Social Responsibility Accounting focuses solely on the economic effects of business decisions.

Which of the statements are correct?

(A) 1 and 4 only.
(B) 2 and 3 only.
(C) 1, 2, and 3 only.
(D) 2, 3, and 4 only.

Ans :

(B) 2 and 3 only.
Stewardship accounting is the earliest phase, not a modern one. Cost accounting did emerge from the needs of the Industrial Revolution for cost control. Management accounting is correctly described as forward-looking and flexible. Social Responsibility Accounting considers social and environmental effects, not just economic ones. Thus, only statements 2 and 3 are correct.

May/June 2019

130. Consider the following:
Assertion (A): Accounting Standard-1 (AS-1) requires that all significant accounting policies adopted should be disclosed.
Reason (R) : This disclosure facilitates a more meaningful comparison between the financial statements of different enterprises.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
AS-1 mandates the disclosure of all significant accounting policies. The primary reason for this requirement, as stated in the standard's purpose, is to enhance transparency. This allows users to understand the basis on which the financial statements are prepared, which in turn helps facilitate a more meaningful and informed comparison between different enterprises that may use different policies.

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CHAPTER 2

Basic Accountancy Procedures

Oct/Nov 2014

1. According to the chapter's objectives, which of the following aspects of accounting is a key learning outcome for the reader?
   (A) The methods for advanced corporate tax planning and optimization.
   (B) The importance and necessity for uniformity in accounting practices.
   (C) The detailed procedures for international trade finance documentation.
   (D) The complex techniques for algorithmic stock market trading.

   Ans :

   (B) The importance and necessity for uniformity in accounting practices.
   The objectives listed at the beginning of the unit explicitly state that after studying the unit, the reader should be able to appreciate the importance and necessity for uniformity in accounting practices. This ensures that the language of business is commonly understood, promoting comparability and intelligibility across different entities and periods, as discussed in the introduction.

May/June 2005

2. What is cited as a serious problem when dealing with the framework of accounting theory?
   (A) The differences in terminology used by different writers.
   (B) The universal lack of professional accounting bodies.
   (C) The constant changes in government regulations.
   (D) The general absence of technology in recording transactions.

   Ans :

   (A) The differences in terminology used by different writers.
   The introduction highlights that, similar to language having many dialects, accounting also has differences in terminology. It states that one is confronted with a serious problem arising from these differences, where various writers use different words to express the same idea, leading to confusion in the theoretical framework of accounting before standards are applied.

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Oct/Nov 2020

3. The fundamental ideas or basic assumptions underlying the theory and practice of financial accounting are collectively described as what?
   (A) Generally Accepted Auditing Standards (GAAS).
   (B) International Financial Reporting Standards (IFRS).
   (C) Broad working rules for all accounting activities.
   (D) Corporate governance and business ethics codes.

   Ans :

   (C) Broad working rules for all accounting activities.
   The text states that the basic rules for recording transactions are fundamental ideas or basic assumptions that form the broad working rules for all accounting activities. These rules, developed and accepted by the accounting profession, are based on experience, reason, usage, and necessity, serving as the foundation for the theory and practice of financial accounting.

May/June 2018

4. The chapter classifies accounting concepts under two broad heads for study. What are these two heads?
   (A) Concepts for Assets and Concepts for Liabilities.
   (B) Concepts for Internal Reporting and Concepts for External Reporting.
   (C) Concepts for Manufacturing and Concepts for Service industries.
   (D) Concepts at the Recording Stage and Concepts at the Reporting Stage.

   Ans :

(D) Concepts at the Recording Stage and Concepts at the Reporting Stage.
The introduction explicitly organizes the study of accounting concepts under two broad heads. The provided table clearly delineates these categories as 'At the Recording Stage' and 'At the Reporting Stage'. This classification helps in understanding when each concept is primarily applied during the accounting process, from initial transaction entry to final report preparation.

Oct/Nov 2012

5. Based on the provided classification, which of the following is a concept applicable at the 'Reporting Stage' of accounting?
(A) Money measurement concept
(B) Business entity concept
(C) Convention of Materiality
(D) Dual aspect concept

Ans :

(C) Convention of Materiality.
The table presented in the introductory section distinctly categorizes various accounting concepts. The Convention of Materiality is listed under the heading 'At the Reporting Stage', alongside concepts like Going Concern and Matching Concept. The other options—Money measurement, Business entity, and Dual aspect—are all listed under the 'At the Recording Stage' category.

May/June 2025

6. Which of the following is listed as an accounting concept to be observed 'At the Recording Stage'?
(A) Matching concept
(B) Realisation concept
(C) Convention of Conservatism
(D) Convention of Consistency

Ans :

(B) Realisation concept.
According to the classification of accounting concepts, the Realisation concept is observed 'At the Recording Stage'. This is the stage where transactions are initially entered into the books. The Matching concept, Convention of Conservatism, and Convention of Consistency are all listed as concepts and conventions to be observed 'At the Reporting Stage' of financial statement preparation.

Oct/Nov 2007

7. Which of the following is NOT a term used to describe the basic ideas of accounting?
(A) Postulates
(B) Propositions
(C) Doctrines
(D) Hypotheses

Ans :

(D) Hypotheses.
The text lists various terms used for describing the basic ideas of accounting. These include concepts, postulates, propositions, basic assumptions, underlying principles, fundamentals, conventions, doctrines, and rules. The term 'Hypotheses' is not mentioned in this specific list, making it the correct answer as it is not one of the described terminologies in this context.

May/June 2010

8. How is 'Accountancy' defined in the chapter?
(A) The systematic knowledge of accounting and the methods for preparing financial records.
(B) The formal process of auditing financial statements to verify their accuracy and check for material misstatements.
(C) The comprehensive legal framework governing business transactions, contracts, and corporate compliance obligations.
(D) The specific, procedural act of simply recording the day-to-day financial transactions of a business enterprise.

Ans :

(A) The systematic knowledge of accounting and the methods for preparing financial records.
The chapter defines 'Accountancy' as the systematic knowledge of accounting. It further elaborates that accountancy explains the method of preparing the books of accounts and summarizing and communicating accounting information. It is the theoretical body of knowledge, while accounting is the practical application of that knowledge, guided by accounting principles and standards.

Oct/Nov 2015

9. Accounting is often referred to as the "language of business" because it is the medium through which a business house communicates with whom?
(A) Only its internal stakeholders, such as top-

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level management.
(B) Only external regulatory bodies, such as government and tax authorities.
(C) The outside world, including investors, creditors, and other stakeholders.
(D) Primarily with other firms in the industry, such as its competitors.

Ans :

(C) The outside world, including investors, creditors, and other stakeholders.
The text states that accounting is often called the language of business because it is the channel through which a business house normally communicates with the outside world. To make this communication intelligible and commonly understood by all parties, it must be based on certain uniform, scientifically laid down standards, which are known as accounting principles.

May/June 2022

10. What are 'accounting principles' defined as in the chapter?
(A) The body of doctrines associated with the theory and procedure of accounting.
(B) A strict set of laws enacted by the government that all businesses must follow.
(C) Optional guidelines that companies can choose to adopt or completely ignore.
(D) A specific software program used for automated bookkeeping and financial reporting.

Ans :

(A) The body of doctrines associated with the theory and procedure of accounting.
The chapter provides a specific definition for accounting principles as 'the body of doctrines commonly associated with the theory and procedure of accounting, serving as an explanation of current practices and as a guide for the selection of conventions or procedures where alternatives exist'. These principles establish standards for sound accounting practices and financial reporting.

Oct/Nov 2006

11. What is the fundamental rule of the Cost Concept in accounting?
(A) All transactions are recorded at their future expected value.
(B) All transactions are recorded at the prevailing market price.
(C) Only transactions involving cash are recorded at their cost price.
(D) All business transactions are recorded in the books at cost price.

Ans :

(D) All business transactions are recorded in the books at cost price.
The Cost Concept, also known as the historical cost concept, dictates that every business transaction must be recorded in the books of accounts at its original cost price, regardless of its current market value. This cost serves as the basis for all subsequent accounting for the asset throughout its life in the business.

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May/June 2014

12. A company purchases machinery. According to the Cost Concept, what amount should be recorded in the books?
(A) The original list price quoted by the supplier, excluding any discounts or additional installation charges.
(B) The purchase price plus all necessary costs incurred for acquisition and installation.
(C) The assessed current market value of the machinery at the balance sheet date, reflecting its present worth.
(D) The estimated future salvage or resale value of the machinery at the end of its projected useful life.

Ans :

(B) The purchase price plus all necessary costs incurred for acquisition and installation.
The chapter uses the example of machinery to illustrate the Cost Concept. It specifies that the machinery is recorded by the amount paid to the supplier plus any additional expenses incurred to bring and install it, which are necessary to put the asset in working order. This total amount constitutes its historical cost.

Oct/Nov 2019

13. Which of the following is a direct application of the Cost Concept?
(A) Fixed assets are periodically revalued to reflect their current market price.
(B) Unrealised gains from holding an asset are recorded as business income.
(C) An item without an acquisition cost is not recorded in the books.

(D) Transactions are recorded based on their estimated future worth.

Ans :

(C) An item without an acquisition cost is not recorded in the books.
The chapter lists four key applications of the Cost Concept. One of these applications is that an item that has no cost is not recorded in the books. This is because the concept requires a transaction to be recorded at the price paid or cost incurred to acquire it; without a cost, there is no value to record.

May/June 2008

14. Which of the following statements about the Cost Concept is incorrect?
(A) It states that an asset is worth the price paid to acquire it.
(B) The term 'book value' refers to the amount shown in the accounting records.
(C) The cost of an asset is the basis for all subsequent accounting for it.
(D) Assets shown on financial statements necessarily indicate their present market worth.

Ans :

(D) Assets shown on financial statements necessarily indicate their present market worth.
The chapter explicitly states that assets shown on financial statements do not necessarily indicate their present market worth. This is described as being contrary to what an uninformed person might believe. The cost concept dictates that assets are recorded at historical cost, which often differs significantly from current market value, especially for long-held assets.

Oct/Nov 2024

15. In the context of the Cost Concept, what does the term 'book value' represent?
(A) The amount shown for an asset in the accounting records.
(B) The current market value of an asset.
(C) The liquidation value of an asset.
(D) The original price of an asset without considering depreciation.

Ans :

(A) The amount shown for an asset in the accounting records.
The text clarifies the terminology used in accounting records. It specifies that the term 'book value' is used for the amount shown in the accounting records for an asset. This value originates from the historical cost and is systematically reduced over time for depreciable assets, distinguishing it from the asset's current market or replacement value.

May/June 2016

16. According to the chapter, what is the general relationship between the accounting value and market value of an asset?
(A) The accounting value and market value are always maintained to be identical through frequent adjustments.
(B) The longer an asset is held, the less likely its book value will match its market value.
(C) The longer an asset is held, the more likely its book value will converge with its market value due to depreciation.
(D) The accounting value is consistently and systematically kept higher than the prevailing market value.

Ans :

(B) The longer an asset is held, the less likely its book value will match its market value.
The chapter explains that while for some assets like cash, accounting and market values might be similar, this is not generally the case. It explicitly states that the longer an asset has been owned by the company, the lesser are the chances that the accounting value (based on historical cost) will correspond to the market value.

Oct/Nov 2011

17. How does the chapter describe the process of 'depreciation'?
(A) A valuation process to adjust an asset's book value to its current fair market value each period.
(B) A systematic allocation of an asset's cost to expense over its useful life.
(C) A funding method for setting aside cash reserves to purchase a replacement asset at the end of its life.
(D) An accounting process to record the increase in value (appreciation) of fixed assets like land.

Ans :

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(B) A systematic allocation of an asset's cost to expense over its useful life.

The text defines depreciation as a process by which the cost of an asset with a long but limited life is systematically reduced (or written off). This is achieved by allocating a part of its cost to expense in each accounting period. The purpose is cost allocation, not valuation to market price.

May/June 2020

18. What is the primary purpose of charging depreciation on an asset?

(A) To allocate the cost of an asset over its useful life.
(B) To ensure the asset's book value reflects its fall in market value.
(C) To create a fund for the replacement of the asset.
(D) To record unrealised losses on the asset each year.

Ans :

(A) To allocate the cost of an asset over its useful life.

The chapter explicitly states that the purpose of depreciation is to allocate the cost of an asset over its useful life, not to adjust its cost to bring it closer to the market value. This process systematically matches the cost of the asset with the revenues it helps to generate over several accounting periods.

Oct/Nov 2016

19. What is the relationship between depreciation and the market value of an asset as described in the text?

(A) Depreciation is charged to make the book value equal to the market value.
(B) The amount of depreciation is directly calculated from the change in market value.
(C) There is no relationship between depreciation and changes in the market value of assets.
(D) Depreciation is charged only when the market value of an asset falls below its cost.

Ans :

(C) There is no relationship between depreciation and changes in the market value of assets.

The text makes a clear distinction between depreciation and market value fluctuations. It states that the intention is not to charge depreciation equal to the fall in the market value of the asset and, as such, there is no relationship between depreciation and changes in market value. Depreciation is a cost allocation process.

May/June 2007

20. What are the three basic criteria that the Cost Concept is argued to meet?

(A) Relevance, Objectivity, and Feasibility.
(B) Profitability, Liquidity, and Solvency.
(C) Simplicity, Accuracy, and Timeliness.
(D) Materiality, Consistency, and Prudence.

Ans :

(A) Relevance, Objectivity, and Feasibility.

At the end of the discussion on the Cost Concept, the chapter mentions that the main argument in its favor is that it meets all three basic criteria of relevance, objectivity, and feasibility. The cost is relevant, objectively verifiable from source documents, and feasible to ascertain and record at the time of the transaction.

Oct/Nov 2021

21. Which accounting concept dictates that only transactions expressible in terms of money are recorded in the books of accounts?

(A) Business Entity Concept
(B) Cost Concept
(C) Going Concern Concept
(D) Money Measurement Concept

Ans :

(D) Money Measurement Concept.

The Money Measurement Concept is the principle which states that every transaction recorded in the books must be measured in terms of money. It provides a common denominator for recording heterogeneous factors like buildings, machines, and trucks, allowing for meaningful addition and comparison of different assets and equities in financial statements.

May/June 2012

22. Which of the following is a direct application of the Money Measurement Concept?

(A) The owner's personal transactions are kept separate from business transactions.
(B) Any inflation or deflation is not included in the value of any asset.
(C) All anticipated losses are provided for, but anticipated profits are ignored.
(D) Fixed assets are recorded at their original purchase price.

Ans :

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(B) Any inflation or deflation is not included in the value of any asset.
The chapter lists applications of the Money Measurement Concept. One of these is that inflation or deflation is not included in the value of an asset. This is a consequence of assuming a stable monetary unit, where the value of the currency at the time of the transaction is used without subsequent adjustment for changes in purchasing power.

Oct/Nov 2009

23. As per the Money Measurement Concept, which of the following events would NOT be recorded in a company's books of accounts?
(A) The purchase of raw materials on credit from a key supplier for ₹1,00,000.
(B) The monthly payroll payment for all employee salaries amounting to ₹50,000.
(C) The sale of finished goods to a major customer on credit for ₹25,000.
(D) A significant internal dispute between the production and audit managers.

Ans :

(D) A significant internal dispute between the production and audit managers.
The Money Measurement Concept imposes a limitation that facts, however vital to the business, cannot be recorded if they are not expressible in monetary terms. The text provides the example of a dispute between key managers, which is of great concern but cannot be quantified in money and is therefore omitted from the accounts.

May/June 2023

24. What is identified as the first severe limitation of the Money Measurement Concept?
(A) The inherent difficulty in accurately converting transactions denominated in various foreign currencies.
(B) The tendency to significantly overstate the real value of assets during periods of high deflation.
(C) The requirement for highly complex and time-consuming calculations for every single business transaction.
(D) The omission of vital, non-monetary facts from the accounting records.

Ans :

(D) The omission of vital, non-monetary facts from the accounting records.
The chapter outlines two severe limitations. The first is that many crucial facts, such as the health of a key director, poor labor relations, or the emergence of a superior competitor's product, are not recorded in the books of accounts because they cannot be expressed in monetary terms, leading to an incomplete picture of the business.

Oct/Nov 2018

25. The second limitation of the Money Measurement Concept is its assumption of a stable value of money. This means it ignores changes in what?
(A) The exchange rate of the currency.
(B) The interest rates set by the central bank.
(C) The purchasing power of money.
(D) The company's stock price.

Ans :

(C) The purchasing power of money.
The second limitation discussed is that using money as a unit of measurement implies a stable or constant value. This assumption ignores the reality of inflation or deflation, where the purchasing power of the currency changes over time. Accounting records do not typically get adjusted for these changes, which can distract financial analysis.

May/June 2019

26. What does the chapter suggest as a desirable way to address the problem of changing price levels on financial reporting?
(A) To abandon the money measurement concept entirely.
(B) To present a supplementary analysis showing the effect of price level changes.
(C) To switch to a barter system of accounting.
(D) To only record transactions in a stable foreign currency.

Ans :

(B) To present a supplementary analysis showing the effect of price level changes.
While acknowledging the problem of changing purchasing power, the text notes that few accountants make allowances for it in the primary books. It then suggests that it would be desirable to present a supplementary analysis showing the effect of price level changes on the reported income and financial position of the business.

NODIA

Oct/Nov 2025

27. **Assertion (A) :** The health of a company's managing director, who is a key contributor to its success, is not recorded in the books of accounts.
Reason (R) : The money measurement concept states that only facts expressible in terms of money are recorded in accounting.
(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
The assertion (A) is true, as the chapter uses this specific example. The reason (R) is also true, as it correctly defines the core principle of the money measurement concept. The reason directly explains the assertion because the director's health, while vital, cannot be quantified in monetary terms and is therefore excluded from the accounts.

May/June 2011

28. Which accounting concept separates the entity of the proprietor from the business transactions?
(A) Business Entity Concept
(B) Cost Concept
(C) Realisation Concept
(D) Dual Aspect Concept

Ans :

(A) Business Entity Concept.
The Business Entity Concept is the principle that makes a distinction between the business and its owner(s). The enterprise is treated as an economic unit separate and apart from its owners. Consequently, all records are kept from the viewpoint of the business, not the owner, and the owner's personal transactions are excluded.

Oct/Nov 2010

29. Under the Business Entity Concept, how is the capital contributed by the owner treated by the business?
(A) As an asset.
(B) As revenue.
(C) As a liability.
(D) As an expense.

Ans :

(C) As a liability.
The chapter explains that because the business is considered an artificial person, separate from its owner, the capital contributed by the owner is treated as a liability of the business to the owner. This signifies the business's obligation to its proprietor for the funds invested, reinforcing the separate entity principle.

May/June 2017

30. Which of the following is listed as an application of the Business Entity Concept?
(A) Any money withdrawn by the proprietor is treated separately as drawings.
(B) Fixed assets are valued at cost and not their current market value.
(C) Every transaction is recorded with the present value and not any future value.
(D) All possible losses are considered, while anticipated profits are ignored.

Ans :

(A) Any money withdrawn by the proprietor is treated separately as drawings.
The text lists several applications of the Business Entity Concept. A key application is that any money or goods withdrawn by the proprietor for personal use is treated as 'drawings'. This transaction reduces the business's cash or assets and simultaneously reduces its liability (capital) to the owner, maintaining the separation between business and personal affairs.

Oct/Nov 2022

31. The owner of a grocery shop takes ₹5,000 cash from the business cash box to pay for his child's school fees. From the business's viewpoint, what is the effect of this transaction?
(A) The business has earned an income of ₹5,000, which increases its overall net profit for the period.
(B) The business's cash is reduced, and the ₹5,000 is recorded as a miscellaneous business operating expense.
(C) The transaction is ignored in the business's books, as it makes no net difference to the owner's personal wealth.
(D) A reduction in business cash and a corresponding reduction in the owner's capital claim.

Ans :

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(D) A reduction in business cash and a corresponding reduction in the owner's capital claim.

This scenario illustrates the Business Entity Concept. The business is separate from the owner. When the owner takes cash for personal use, the business's asset (cash) decreases. This withdrawal is treated as 'drawings,' which represents a reduction of the owner's capital or claim against the business, not a business expense.

May/June 2013

32. For accounting purposes, the distinction between business and owner is maintained for which types of enterprises?

(A) Only for limited companies.
(B) For limited companies, partnerships, and sole proprietorships.
(C) Only for partnerships and sole proprietorships.
(D) Only for non-profit organizations.

Ans :

(B) For limited companies, partnerships, and sole proprietorships.

The chapter clarifies that while the distinction is legally clear for a limited company (which has its own legal personality), accounting still maintains this separation for partnerships and sole proprietorships. Even though the law may not make such a distinction for proprietorships, it is a fundamental concept for accounting purposes across these business forms.

Oct/Nov 2005

33. According to the Realisation Concept, when is revenue from the sale of goods considered to be earned?

(A) When the initial purchase order is formally received and acknowledged from the customer.
(B) When the goods are fully manufactured, packaged, and designated as ready for dispatch to the buyer.
(C) When ownership of the goods transfers to the buyer, creating a legal obligation to pay.
(D) When the full cash payment is actually received from the customer for the delivered goods.

Ans :

(C) When ownership of the goods transfers to the buyer, creating a legal obligation to pay.

The Realization Concept specifies the exact point in time when revenue should be recognized. It states that revenue is treated as realized or earned on the date the property in the goods passes to the buyer, creating a legal obligation for the buyer to pay. It is not necessarily tied to cash receipt or order placement.

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May/June 2024

34. How should a business treat goods that have been sent to a customer on an 'approval' basis, according to the Realisation Concept?

(A) They should be immediately included in sales at the full selling price.
(B) They should be recorded as a confirmed sale with a provision for return.
(C) They should be completely removed from all accounting records.
(D) They will not be included in sales but taken at cost only.

Ans :

(D) They will not be included in sales but taken at cost only.

One of the listed applications of the Realization Concept is that goods sold on approval will not be included in sales. Since the buyer has not yet accepted the goods and is not legally liable to pay, a sale has not been realized. The goods remain part of the seller's inventory and are valued at cost.

Oct/Nov 2008

35. Which of the following statements is inconsistent with the Realization Concept?

(A) Revenue from a highly probable future sale is recorded in the current period.
(B) No future income is considered in the current period's accounts.
(C) The earning process should be either complete or very near completion.
(D) Revenue is earned when the buyer becomes legally liable to pay for the goods.

Ans :

(A) Revenue from a highly probable future sale is recorded in the current period.

The Realization Concept explicitly guards against recognizing income that is not yet earned. It states that no future income is considered. Recording revenue from a probable future sale would violate this principle, as the property in

the goods has not passed and the buyer is not yet legally obligated to pay.

May/June 2006

36. The Dual Aspect Concept explains that every business transaction has what effect?

(A) A corresponding positive and negative impact on the period's reported net profit.
(B) A two-fold effect, resulting in equal debit and credit entries.
(C) A simultaneous impact on both the income statement and the balance sheet accounts.
(D) An immediate cash flow effect and a separate, delayed future cash flow effect.

Ans :

(B) A two-fold effect, resulting in equal debit and credit entries.
The Dual Aspect Concept is the foundation of the double-entry bookkeeping system. It posits that every transaction has two effects or aspects. For every transaction, the total amount of debits must equal the total amount of credits, reflecting the two-sided nature of the event (a receiving aspect and a giving aspect).

Oct/Nov 2017

37. If Mr. X starts a business by investing ₹50,000 in cash, how does the Dual Aspect Concept apply to this transaction?

(A) The business has an asset (cash) of ₹50,000 and an offsetting business expense of ₹50,000.
(B) The business has new revenue of ₹50,000 and a corresponding liability (capital) of ₹50,000.
(C) The business has an asset (cash) of ₹50,000 and another asset (owner's equity) of ₹50,000.
(D) An increase in assets (cash) of ₹50,000 and an increase in liabilities (capital) of ₹50,000.

Ans :

(D) An increase in assets (cash) of ₹50,000 and an increase in liabilities (capital) of ₹50,000.
The chapter uses this exact example to illustrate the Dual Aspect Concept. The business receives an asset, which is cash of ₹50,000. Simultaneously, due to the Business Entity Concept, it incurs a liability to the owner, known as capital, for the same amount. Thus, the transaction has two aspects: an increase in assets and an increase in liabilities.

May/June 2009

38. What is the fundamental accounting equation that is a direct consequence of the Dual Aspect Concept?

(A) Assets = Capital - Liability
(B) Assets = Capital + Liability
(C) Assets + Expenses = Revenue + Liability
(D) Capital = Assets + Liability

Ans :

(B) Assets = Capital + Liability
The Dual Aspect Concept establishes that for every transaction, the total assets of a business must always be equal to its total equities (liabilities + capital). This relationship is expressed in the fundamental accounting equation: Assets = Capital + Liability. Every transaction maintains the balance of this equation, as one aspect is a debit and the other a credit.

Oct/Nov 2013

39. What is the underlying assumption of the Historical Records Concept?

(A) The assumption of consistency.
(B) The assumption of materiality.
(C) The assumption of realisations.
(D) The assumption of prudence.

Ans :

(C) The assumption of realisations.
The text states that the Historical Records Concept is based on the assumption of realizations. This means that accounting involves recording business transactions that have already taken place and have been 'realized'. It focuses on recording past events, not speculating on future transactions that have not yet occurred and cannot be measured accurately.

May/June 2015

40. According to the Historical Records Concept, how are business transactions recorded?

(A) They are recorded as and when they take place, in a date-wise manner.
(B) They are recorded based on their expected future impact.
(C) They are recorded only at the end of the financial year.
(D) They are grouped by type rather than by date of occurrence.

Ans :

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(A) They are recorded as and when they take place, in a date-wise manner.
The Historical Records Concept implies that accounting is a record of past happenings. The chapter explains that business transactions are recorded as and when they occur, i.e., date-wise. This practice leads to the creation of a chronological, historical record of all transactions, ensuring that events are captured accurately as they happen.

Oct/Nov 2023

41. Consider the following statements regarding the Dual Aspect concept:
Statement I : It explains that every transaction has a single effect on the business.
Statement II : The fundamental accounting equation derived from it is Assets = Capital + Liability.
(A) Only Statement I is correct.
(B) Only Statement II is correct.
(C) Both Statement I and Statement II are correct.
(D) Both Statement I and Statement II are incorrect.

Ans :

(B) Only Statement II is correct.
Statement I is incorrect; the dual aspect concept explains that every transaction has a double or two-fold effect (a debit and a credit). Statement II is correct; the chapter explicitly states that the accounting equation Assets = Capital + Liability is an application of this concept, reflecting the two sides of every transaction.

May/June 2021

42. If an expense is incurred and its utility is consumed during the year, how is it treated under the Going Concern Concept?
(A) It is recorded as an asset.
(B) It is recorded as an expense.
(C) It is recorded as a liability.
(D) It is ignored until it is paid in cash.

Ans :

(B) It is recorded as an expense.
The Going Concern Concept helps differentiate between assets and expenses. The chapter explains that if an expense is incurred and its benefit or utility is fully consumed within the current accounting year, it is treated as an expense for that period. If its utility extends to future periods, it is recorded as an asset.

Oct/Nov 2014

43. Which of the following practices is a direct application of the Going Concern Concept?
(A) Valuing inventory at the lower of cost or market price.
(B) Disclosing all material information in the notes to accounts.
(C) Writing off deferred revenue expenditures over a number of years.
(D) Recording only transactions that can be measured in money.

Ans :

(C) Writing off deferred revenue expenditures over a number of years.
The Going Concern assumption implies the business will continue to operate for the foreseeable future. This justifies spreading the cost of certain large expenditures, known as deferred revenue expenditures, over the several years that will benefit from them. The list of applications explicitly includes that "Deferred revenue expenditures are written off over a number of years."

May/June 2005

44. The practice of providing depreciation on fixed assets based on their total useful life is justified by which accounting concept?
(A) Money Measurement Concept
(B) Business Entity Concept
(C) Realisation Concept
(D) Going Concern Concept

Ans :

(D) Going Concern Concept.
The Going Concern Concept assumes that the business will continue its operations long enough to utilize its fixed assets for their entire useful lives. This assumption provides the basis for systematically allocating the cost of an asset (depreciation) over its life, rather than expensing it immediately or valuing it at its liquidation price.

Oct/Nov 2020

45. Which of the following statements about the Going Concern concept are correct?
1. It assumes the business entity has an infinite life.
2. It justifies valuing fixed assets at cost instead of market value.
3. It leads to the creation of reserves and

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provisions for future liabilities.
(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(D) 1, 2, and 3.
The chapter's list of applications for the Going Concern concept supports all three statements. It helps investors assume the life of the business is infinite, it justifies valuing fixed assets at cost, and it is the basis for creating reserves and provisions for future liabilities, as the business is expected to be around to meet them.

May/June 2018

46. The Matching Concept explains that the income of a certain period must be matched with what?
(A) The assets of that period only.
(B) The expenses of that period only.
(C) The liabilities of that period only.
(D) The cash receipts of that period only.

Ans :

(B) The expenses of that period only.
The Matching Concept is a principle of accrual accounting that dictates the determination of periodic profit. It requires that the revenues generated during an accounting period are matched with the expenses incurred to generate those revenues, regardless of the timing of the actual cash flows associated with them.

Oct/Nov 2012

47. The justification for the Matching Concept is said to arise from which other accounting concept?
(A) The Business Entity Concept
(B) The Dual Aspect Concept
(C) The Money Measurement Concept
(D) The Accounting Period Concept

Ans :

(D) The Accounting Period Concept.
The text explicitly states, "The justification of the matching concept arises from accounting period concept." The Accounting Period Concept divides the life of a business into shorter, artificial periods. To determine the profit or loss for such a period, the Matching Concept is applied to correctly associate the revenues and expenses belonging to it.

May/June 2025

48. Making adjustments for outstanding expenses and prepaid expenses in the final accounts is an application of which concept?
(A) The Matching Concept
(B) The Cost Concept
(C) The Conservatism Concept
(D) The Materiality Concept

Ans :

(A) The Matching Concept.
The chapter lists applications of the Matching Concept, which include making all adjustments for prepaid and outstanding expenses. This ensures that only the expenses related to the current accounting period are charged against the revenues of that period, providing a more accurate measurement of profit or loss for that specific timeframe.

Oct/Nov 2007

49. Why is the Accounting Period Concept considered necessary in accounting?
(A) Because it is a specific and non-negotiable legal requirement for all business types in all countries.
(B) To allow for the final and precise determination of a business's total profit over its entire lifetime.
(C) Because stakeholders need periodic performance results and cannot wait for the business's liquidation.
(D) To ensure all business assets are re-evaluated and recorded at their current market value at regular intervals.

Ans :

(C) Because stakeholders need periodic performance results and cannot wait for the business's liquidation.
The chapter explains that while the precise results of an enterprise are known only upon its liquidation, interested parties like owners, management, and creditors cannot wait that long. The Accounting Period Concept addresses this need by forcing the accountant to report on the firm's performance and financial position for shorter, regular intervals.

May/June 2010

50. What is the most common interval used for external financial reporting, according to the chapter?

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(A) One year
(B) One month
(C) Three months (a quarter)
(D) Six months

Ans :

(A) One year.
The text states that while periods in practice vary, "a year is the most common interval" for external reporting. This is attributed to established business practice, tradition, and government requirements (such as for tax purposes). Shorter intervals like one or three months are mentioned as being more common for internal reporting purposes.

Oct/Nov 2015

51. What is a 'natural' business year defined as?
(A) The twelve-month period from January 1st to December 31st.
(B) The twelve-month period from April 1st to March 31st.
(C) A twelve-month period ending at the point of the lowest volume of business activity.
(D) Any period of time that the business owner decides is natural for the business.

Ans :

(C) A twelve-month period ending at the point of the lowest volume of business activity.
The chapter introduces the concept of a 'natural' business year, which more and more firms are adopting. It is defined as a twelve-month period where the end is marked by the relatively lower or lowest volume of business activity. This often makes year-end procedures like inventory counting easier and more accurate.

May/June 2022

52. According to the principles stemming from the Accounting Period Concept, how are revenues and costs treated when preparing periodic financial statements?
(A) Only revenues and costs received or paid in cash are included.
(B) All revenues and costs relating to the year are taken into account, irrespective of cash movement.
(C) Only costs are taken into account, while revenues are deferred to the next period.
(D) Only revenues are taken into account, while costs are capitalized as assets.

Ans :

(B) All revenues and costs relating to the year are taken into account, irrespective of cash movement.
The text clarifies that while matching earnings and costs for a period, all revenues and costs relating to the year in question are considered, regardless of whether they have been received in cash or paid in cash. This is the essence of accrual accounting, which is facilitated by the accounting period and matching concepts.

Oct/Nov 2006

53. Which of the following is an application of the Accounting Period Concept?
(A) Valuing stock at the lower of cost or market value.
(B) Enabling tax calculation and dividend distribution on a periodic basis.
(C) Treating the business as separate from its owner.
(D) Recording transactions at their historical cost.

Ans :

(B) Enabling tax calculation and dividend distribution on a periodic basis.
The chapter lists four applications of the Accounting Period Concept. One of these is that it "Enables tax calculation and dividend distribution." By creating defined periods like a financial year, the concept provides a basis for calculating annual profits, upon which taxes are levied and from which dividends can be appropriately distributed to shareholders.

May/June 2014

54. The Convention of Full Disclosure implies that accounts must be honestly prepared and that:
(A) Only information favorable to the business should be disclosed.
(B) Secret reserves should be created to strengthen the financial position.
(C) All information, regardless of significance, must be disclosed in detail.
(D) All material information must be disclosed.

Ans :

(D) All material information must be disclosed.
The Convention of Full Disclosure requires that financial statements and their accompanying notes provide all material information relating

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to the business's activities. The goal is honest preparation and transparency, preventing the concealment of important facts from outsiders. It specifically mentions that secret reserves should not be maintained, as this would violate the principle of full disclosure.

Oct/Nov 2019

55. The practice of appending notes to financial statements to report contingent liabilities is an application of which accounting convention?
(A) Convention of Conservatism
(B) Convention of Consistency
(C) Convention of Full Disclosure
(D) Convention of Materiality

Ans :

(C) Convention of Full Disclosure.
The text provides specific examples of the application of the Convention of Full Disclosure. It mentions that the practice of appending notes relating to various facts or items that do not find a place in the main accounting statements, such as contingent liabilities and the market value of investments, is done in pursuance of this convention.

May/June 2008

56. Which statement is incorrect regarding the Convention of Full Disclosure?
(A) It implies that accounts must be honestly prepared.
(B) It encourages the maintenance of secret reserves for financial stability.
(C) The Indian Companies Act makes provisions for the disclosure of essential information.
(D) It aims to make all material facts compulsory for disclosure.

Ans :

(B) It encourages the maintenance of secret reserves for financial stability.
The chapter explicitly states that as per the Convention of Full Disclosure, "Secret reserves should not be maintained." The purpose of this convention is to ensure transparency and provide honest information to outsiders. Creating secret reserves would conceal the true financial position and is therefore contrary to the principle of full and fair disclosure.

Oct/Nov 2024

57. According to the Convention of Materiality, what does the materiality of an item depend upon?
(A) Only on the monetary value of the item.
(B) The personal judgment of the bookkeeper alone.
(C) Whether the item represents an asset or a liability.
(D) The value of the item and the circumstances of the individual case.

Ans :

(D) The value of the item and the circumstances of the individual case.
The chapter explains that what is considered material is not based on a fixed rule but depends on the specific situation. It states that materiality depends upon the value of the item involved and the circumstances of the individual case of the business. An amount that is material for a small business may be immaterial for a large corporation.

May/June 2016

58. As per Ind AS-1, how can an entity treat items of a dissimilar nature or function?
(A) They need not be presented separately if they are immaterial.
(B) They must always be presented separately, regardless of their value.
(C) They must be grouped together under a "miscellaneous" heading.
(D) They should be excluded from the financial statements entirely.

Ans :

(A) They need not be presented separately if they are immaterial.
The text cites Ind AS-1 as an application of the materiality convention. It states that Ind AS-1 allows an entity to not present dissimilar items separately if those items are immaterial. This practical exception prevents financial statements from being cluttered with trivial details, focusing the user's attention on significant information that could influence decisions.

Oct/Nov 2011

59. A large bank purchases a paper stapler for ₹30. The stapler is expected to last for three years. According to the Convention of Materiality, how should the bank's accountant treat this expenditure?

NODIA

(A) Capitalize it as a fixed asset and systematically depreciate it over its three-year useful life.
(B) Record the purchase as a short-term marketable investment to be sold at a later date for a gain.
(C) Ignore the ₹30 transaction completely in the books as the purchase amount is de minimis.
(D) Treat the entire ₹30 as an expense in the current period.

Ans :

(D) Treat the entire ₹30 as an expense in the current period.
The chapter uses this exact example to illustrate materiality. Although theoretically the stapler is an asset, its cost is trivial for a large entity. The effort involved in capitalizing and depreciating it over three years is not justified by the benefit. Therefore, the concept of materiality allows the accountant to treat it as an expense immediately.

May/June 2020

60. At the end of an accounting period, a company has a small amount of unused stationery in stock. Treating the entire stationery purchase for the year as an expense, rather than carrying the unused portion forward as an asset, is an application of which concept?
(A) Going Concern
(B) Full Disclosure
(C) Materiality
(D) Consistency

Ans :

(C) Materiality.
This scenario is explicitly discussed in the chapter. The accountant would regard the small stock of unused stationery as immaterial. Therefore, instead of treating it as an asset to be carried forward, the entire amount spent on stationery during the period is expensed. This practical shortcut is justified by the materiality concept.

Oct/Nov 2016

61. **Assertion (A) :** The cost of recording and reporting trivial business events may not be justified by the usefulness of the information derived.
Reason (R) : The Materiality concept holds that items of small significance need not be given a strictly theoretically correct treatment.
(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
Assertion (A) correctly states the cost-benefit consideration for small items. Reason (R) correctly defines the principle of the Materiality concept. The reason (R) provides the direct justification for the assertion (A), as the materiality concept is the accounting principle that allows for practical, cost-effective treatment of insignificant items, overriding strict theoretical rules.

May/June 2007

62. The Convention of Conservatism is also known by what other name?
(A) The Principle of Materiality
(B) The Principle of Prudence
(C) The Principle of Objectivity
(D) The Principle of Entity

Ans :

(B) The Principle of Prudence.
The text explicitly states that the Convention of Conservatism is "also called the principle of prudence." This principle advocates for a cautious approach in accounting, especially when dealing with uncertainty. It involves recognizing potential losses while not anticipating profits, ensuring that financial statements do not overstate the entity's financial health.

Oct/Nov 2021

63. Which phrase best summarizes the Convention of Conservatism?
(A) Record all assets and transactions at their original, verifiable historical cost.
(B) Disclose all material financial information that could influence a user's decision.
(C) Anticipate no profit, provide for all possible losses.
(D) Apply the same accounting principles and methods consistently from one year to the next.

Ans :

(C) Anticipate no profit, provide for all possible losses.

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The chapter quotes this exact phrase, "'anticipate no profit, provide for all possible losses'", as the common statement of the Convention of Conservatism or Prudence. This guiding rule means accountants should adopt a cautious stance, recognizing liabilities and expenses as soon as they are possible but recognizing revenues and assets only when they are assured.

May/June 2012

64. The creation of a provision for doubtful debts is an application of which accounting convention?
(A) Convention of Consistency
(B) Convention of Full Disclosure
(C) Convention of Materiality
(D) Convention of Conservatism

Ans :

(D) Convention of Conservatism.
The chapter lists the "Creation of provisions for doubtful debts" as the first application of the Convention of Conservatism. This practice involves recognizing a potential loss from customers who may not pay their dues, even before that loss is certain. It is a classic example of providing for a possible loss in line with the principle of prudence.

Oct/Nov 2009

65. According to the Convention of Conservatism, how should inventory (stock in hand) be valued?
(A) At the lower of cost or market value.
(B) At cost price only.
(C) At market value only.
(D) At the higher of cost or market value.

Ans :

(A) At the lower of cost or market value.
A key application of the principle of conservatism listed in the text is to "Value the stock in hand at lower of the cost or market value." This ensures that if the market value has fallen below cost, the potential loss is recognized immediately, while any unrealized gain (if market value is above cost) is ignored.

May/June 2023

66. What does the Convention of Consistency require from a company?
(A) To use the most profitable accounting method available.
(B) To regularly follow the same accounting method for recording and reporting similar events.
(C) To change accounting methods every year to provide different perspectives.
(D) To apply the same accounting method across all different types of transactions.

Ans :

(B) To regularly follow the same accounting method for recording and reporting similar events.
The Convention of Consistency requires that once a company selects a specific accounting method for a particular type of transaction (e.g., depreciation or inventory valuation), it must continue to use that same method for all subsequent events of the same character. This ensures that financial statements are comparable over time.

Oct/Nov 2018

67. A company has been using the straight-line method of depreciation for its machinery for the past five years. What does the Convention of Consistency imply for this company?
(A) It must switch to the written-down value method in the sixth year.
(B) It should stop charging depreciation to increase profits.
(C) It can change the method without any specific disclosure.
(D) It should continue to use the straight-line method in the future.

Ans :

(D) It should continue to use the straight-line method in the future.
The chapter uses the example of choosing a depreciation method to illustrate consistency. The convention requires that if the straight-line method is chosen, it should be followed regularly in the future. This allows for meaningful comparison of financial results from one year to the next, as the basis of calculation remains the same.

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May/June 2019

68. If a company, for valid reasons, changes an accounting method it has been following, what is required by the Convention of Consistency?
(A) The financial effect of the change must be disclosed in the financial statements.
(B) The company must seek and receive formal approval from all of its direct competitors.

(C) The change is strictly not permitted under any circumstances once a method is chosen.
(D) The company is required to retroactively restate all prior years' financial statements with the new method.

Ans :

(A) The financial effect of the change must be disclosed in the financial statements.
The Convention of Consistency does not forbid changes in accounting methods absolutely. It allows for changes if there is a sound reason. However, it mandates that if a departure from the existing method is made, "the effect of the change must be clearly stated in the financial statements in the year of change."

Oct/Nov 2025

69. What is the primary utility of accounting information that the Convention of Consistency helps to preserve?
(A) Accuracy
(B) Timeliness
(C) Comparability
(D) Objectivity

Ans :

(C) Comparability.
The text emphasizes that the utility of accounting information lies in the ability to draw valid conclusions from comparing data across different years. "Comparability is essential, so that trends or differences may be identified and evaluated." Inconsistency in methods would undermine this comparability, making analysis of performance over time unreliable.

May/June 2011

70. According to the chapter, inconsistency in the application of accounting methods opens the door for what potential problem?
(A) The potential for manipulating reported income and assets.
(B) A significant and unavoidable increase in annual external audit fees.
(C) Direct conflicts with mandatory international accounting and reporting standards.
(D) A noticeable slowdown in the daily processing and recording of transactions.

Ans :

(A) The potential for manipulating reported income and assets.
The chapter warns that besides affecting comparability, "inconsistency also opens the door for the manipulation of reported income and assets." By switching between different acceptable accounting methods, management could potentially choose the method that presents a more favorable, but not necessarily more accurate, picture of the company's performance or position.

Oct/Nov 2010

71. Which of the following is NOT an application of the Convention of Conservatism?
(A) Creation of contingency reserve.
(B) Showing joint life policy at surrender value on the assets side.
(C) Creation of provisions for doubtful debts.
(D) Recording unrealized gains as soon as they are anticipated.

Ans :

(D) Recording unrealized gains as soon as they are anticipated.
The core idea of conservatism is to anticipate no profits but provide for all possible losses. Recording unrealized gains would be the opposite of this principle. The other three options—creating a contingency reserve, valuing a JLP at surrender value, and creating provisions for doubtful debts—are all examples of cautious accounting that are listed as applications of conservatism.

May/June 2017

72. Consider the following statements regarding the Convention of Consistency:
Statement I : It requires a company to use the same accounting method for all subsequent events of the same character.
Statement II : If a change in method is made, its impact must be disclosed separately.
(A) Only Statement I is correct.
(B) Only Statement II is correct.
(C) Both Statement I and Statement II are correct.
(D) Both Statement I and Statement II are incorrect.

Ans :

(C) Both Statement I and Statement II are correct.
Both statements accurately reflect the principles of the Convention of Consistency as described in the chapter. Statement I defines the core requirement of using a method regularly.

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Statement II describes the mandatory disclosure requirement if a company, for valid reasons, departs from the method it has been following, ensuring transparency for users of the financial statements.

Oct/Nov 2022

73. The Going Concern concept assumes that an enterprise will continue to operate for a long time in the future unless what is true?
(A) The enterprise is not making a profit.
(B) There is good evidence to the contrary.
(C) The enterprise is more than 10 years old.
(D) The management decides to change its product line.

Ans :

(B) There is good evidence to the contrary.
The chapter defines the Going Concern concept as the assumption that the business will continue to operate for a long time "unless there is good evidence to the contrary." This means the default assumption is continuity, but it can be rebutted if there are clear indications of impending liquidation or cessation of trade.

May/June 2013

74. The promoters of a new company know that they will wind it up after exactly four years. How should the depreciation of its tangible assets with a useful life of ten years be accounted for?
(A) Depreciation should be spread over their useful life of ten years.
(B) No depreciation should be charged as the company is temporary.
(C) The depreciation amount should be spread over the next four accounting years.
(D) Depreciation should be charged fully in the first year of operation.

Ans :

(C) The depreciation amount should be spread over the next four accounting years.
This scenario is a direct example used in the text. Since the business is not a going concern beyond four years, the standard application of depreciation over the asset's full useful life is inappropriate. Instead, the cost of the assets must be amortized over the actual expected life of the business, which is four years.

Oct/Nov 2005

75. In which of the following situations is accounting NOT based on the "Going Concern" basis?
(A) A business entity formed for the execution of a specific project, like building a bridge.
(B) A well-established retail company.
(C) A new technology start-up with plans for expansion.
(D) A manufacturing firm that incurred a small loss in the current year.

Ans :

(A) A business entity formed for the execution of a specific project, like building a bridge.
The chapter explicitly mentions that certain business entities are formed for specific projects (e.g., construction of a bridge) and are intended to be dissolved upon project completion. In such cases, the accounting is not based on the "Going Concern" basis because the entity has a definite and limited lifespan from its inception.

May/June 2024

76. According to standard accounting principles, when must an entity prepare financial statements on a basis other than going concern?
(A) Whenever the entity makes a loss for two consecutive years.
(B) If management intends to liquidate the entity or cease trading, or has no realistic alternative.
(C) If the entity is planning a major business expansion.
(D) As soon as the entity's total liabilities exceed its total assets.

Ans :

(B) If management intends to liquidate the entity or cease trading, or has no realistic alternative.
The quoted text from Ind AS-1 is very specific. It states that an entity shall prepare financial statements on a going concern basis "unless management either intends to liquidate the entity or cease trading, or has no realistic alternative except to do so." This sets a high threshold for departing from the going concern assumption.

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Oct/Nov 2008

77. According to standard accounting principles, what must an entity do if it does not prepare financial statements on a going concern basis?
(A) It must seek special permission from the regulatory authorities.

(B) It must immediately sell all its assets at market value.
(C) It must disclose that fact, the basis used, and the reason for not being a going concern.
(D) It is prohibited from distributing any dividends to its shareholders.

Ans :

(C) It must disclose that fact, the basis used, and the reason for not being a going concern.
The Ind AS-1 quote clearly outlines the disclosure requirements in this situation. It says, "it shall disclose that fact, together with the basis on which it prepared the financial statements and the reason why the entity is not regarded as a going concern." This ensures full transparency to the users of the statements.

May/June 2006

78. The assumption that a business is not expected to be liquidated in the foreseeable future establishes the basis for many valuations and allocations in accounting, such as:
(A) Depreciation procedures.
(B) Market valuation procedures.
(C) Liquidation valuation procedures.
(D) Cash flow forecasting procedures.

Ans :

(A) Depreciation procedures.
The text explicitly states that the assumption of continuity "establishes the basis for many of the valuations and allocations in accounting. For example, depreciation (or amortisation) procedures rest upon this concept." Spreading the cost of an asset over its useful life only makes sense if the business is expected to exist for that duration.

Oct/Nov 2017

79. Under what circumstances would it be appropriate for an accountant to report a business's resources at their current or liquidation values?
(A) When the business is experiencing a period of high profitability and rapid growth.
(B) When there is strong evidence the business will cease operations in the near future.
(C) At the end of every accounting year, as part of standard closing procedures for all companies.
(D) When the business successfully acquires a major new asset or a subsidiary company.

Ans :

(B) When there is strong evidence the business will cease operations in the near future.
The chapter concludes the section on going concern by noting the exception to the rule. If the accountant has good reasons to believe the business is going to be liquidated or will cease operations soon (e.g., within a year or two), the historical cost basis is no longer relevant. In such cases, resources should be reported at current or liquidation values.

May/June 2009

80. Which of the following describes a key feature of the single entry system of bookkeeping?
(A) Partial or incomplete recording of transactions, with some being omitted entirely.
(B) It is based on rigorous scientific principles and is considered highly reliable for reporting.
(C) It meticulously records both the debit and credit aspects of each and every transaction.
(D) It is the standard, mandatory system used by most large, publicly traded business houses.

Ans :

(A) Partial or incomplete recording of transactions, with some being omitted entirely.
The text describes the single entry system as unscientific. Its primary characteristic is that it does not follow the dual aspect principle systematically. As a result, "some transactions are not recorded at all, whereas some other transactions are recorded only partially," leading to incomplete and unreliable accounting records.

Oct/Nov 2013

81. Why is the single entry system considered to be unreliable?
(A) Because it is too complex for small business firms.
(B) Because it requires the use of expensive accounting software.
(C) Because it focuses too much on nominal and real accounts.
(D) Because the accounts maintained are incomplete and unsystematic.

Ans :

(D) Because the accounts maintained are incomplete and unsystematic.

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The chapter states that the accounts maintained under the single entry system are "incomplete and unsystematic and, therefore, the system is not reliable." It primarily focuses on personal accounts (customers, suppliers) and cash, while ignoring or incompletely recording other aspects, making it impossible to prepare a full set of financial statements accurately.

May/June 2015

82. The double entry system of bookkeeping is based on which fundamental concept?
(A) The Materiality Concept
(B) The Dual Aspect Concept
(C) The Conservatism Concept
(D) The Going Concern Concept

Ans :

(B) The Dual Aspect Concept.
The text clearly links the double entry system to the dual aspect concept. It states, "Under the double entry system of bookkeeping, both aspects of each and every transaction are recorded. This is known as the dual aspect analysis." This system recognizes that every transaction has two sides, a debit and a credit.

Oct/Nov 2023

83. According to the chapter, what is "the crux of accountancy"?
(A) The final process of preparing and filing the annual corporate tax returns with the government.
(B) Identifying the two affected accounts and determining which to debit and which to credit.
(C) The periodic revaluation and calculation of the current market value of all business assets.
(D) The high-level strategic task of ensuring the business consistently operates at a significant profit.

Ans :

(B) Identifying the two affected accounts and determining which to debit and which to credit.
The text uses this specific phrase to emphasize the core task in double-entry bookkeeping. It states, "The crux of accountancy lies in finding out which of the two accounts are affected by a particular transaction and out of these two accounts, which account is to be debited and which account is to be credited."

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May/June 2021

84. How is an 'account' defined in the chapter?
(A) A formal legal contract establishing terms between the business and a specific customer or supplier.
(B) The complete annual financial report of the company, including all statements and required disclosures.
(C) A physical file folder used for storing original paper copies of invoices, receipts, and bank statements.
(D) A summary record of transactions for a specific person, asset, liability, income, or expense.

Ans :

(D) A summary record of transactions for a specific person, asset, liability, income, or expense.
To explain the rules of debit and credit, the chapter first defines the term 'account'. It is described as "a summarised record of all transactions relating to a particular person, a thing, or an item of income or expense." This record helps in tracking the changes and final balance for each specific element.

Oct/Nov 2014

85. In the standard 'T' account format, the left-hand side is known as the 'debit side' and is denoted by 'Dr'. What is the right-hand side known as?
(A) The credit side, denoted by 'Cr'.
(B) The asset side, denoted by 'As'.
(C) The balance side, denoted by 'Bal'.
(D) The entry side, denoted by 'En'.

Ans :

(A) The credit side, denoted by 'Cr'.
The chapter describes the physical layout of an account, which is vertically divided like the letter 'T'. It explicitly states that "The right hand side, is known as the 'credit side' and denoted by 'Cr' on the right hand top corner of the account." This is a fundamental convention in bookkeeping.

May/June 2005

86. Which of the following is listed as a main principle of the double entry system?
(A) For every transaction, only one party must be interested.
(B) Every business transaction has two aspects: one of receiving the benefit and the other of giving it.

(C) Only the receiving aspect of a transaction is recorded in the books of account.
(D) The two-fold effect of a transaction is recorded on different dates.

Ans :

(B) Every business transaction has two aspects: one of receiving the benefit and the other of giving it.
The chapter lists four main principles of the double entry system. The second principle states, "Every business transaction has two aspects, one of receiving the benefit and the other of giving it." This receiving and giving duality is the foundation of the debit and credit mechanism used to record transactions under this system.

Oct/Nov 2020

87. The simple phrase "every debit has a corresponding credit" is a concise summary of which system?
(A) Single entry system
(B) Cash basis accounting
(C) Double entry system
(D) Budgetary control system

Ans :

(C) Double entry system.
The chapter explains the principles of the double entry system and simplifies the second principle by stating, "In simple words, 'double entry' system means 'every debit has a corresponding credit'". This fundamental rule ensures that the accounting equation remains in balance after every single transaction is recorded in the books of account.

May/June 2018

88. Which of the following is NOT listed as a merit of the Double Entry System?
(A) It is the most economical and time-saving system available.
(B) It keeps a complete record of business transactions.
(C) It provides a check on the arithmetical accuracy of the accounts.
(D) The balance sheet can be prepared at any specified point of time.

Ans :

(A) It is the most economical and time-saving system available.
The text lists several merits of the double entry system, including keeping complete records, checking arithmetical accuracy, and enabling the preparation of P&L accounts and balance sheets. However, it describes the single entry system as appearing "to be time saving and economical," implying that the more rigorous double entry system is not primarily chosen for these attributes.

Oct/Nov 2012

89. How does the double entry system facilitate a check on the arithmetical accuracy of the accounts?
(A) By ensuring every transaction is reviewed and formally approved by a senior manager before entry.
(B) By using the equality of debits and credits to prepare a trial balance for verification.
(C) By mandating the use of specialized accounting software that automatically prevents all entry errors.
(D) By requiring all accounts and ledgers to be audited for accuracy by an external party on a daily basis.

Ans :

(B) By using the equality of debits and credits to prepare a trial balance for verification.
Merit (b) of the double entry system states that it provides a check on arithmetical accuracy "since every debit has corresponding credit to it and vice versa." This equality of debits and credits allows for the preparation of a trial balance, where the total of all debit balances should equal the total of all credit balances.

May/June 2025

90. The ability to compare purchases, sales, and expenses of a current year with those of previous years is cited as a merit of which system?
(A) The Double Entry System.
(B) The Single Entry System
(C) The Barter System
(D) The Manual Accounting System

Ans :

(A) The Double Entry System.
Merit (d) of the double entry system highlights its utility for control and analysis. It states that the system "makes possible the comparison of purchases as well as sales, expenditure, income, etc., of a current year, with those of the previous years." This comparability is possible because

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the system maintains complete and systematic records.

Oct/Nov 2007

91. Which of the following statements about the Principle of Conservatism is true?
(A) It suggests recording the highest possible values for assets and the lowest possible values for liabilities.
(B) It states that revenues should be recognised as soon as they are anticipated.
(C) It has been universally accepted without any recent challenges to its logic.
(D) It is also known as the convention of prudence and suggests a cautious approach.

Ans :

(D) It is also known as the convention of prudence and suggests a cautious approach.
The chapter explicitly states that the convention of conservatism is also known as the convention of prudence. It advises the accountant to "follow a cautious approach" by anticipating and providing for all possible losses while not anticipating any profits, ensuring that financial statements are not overly optimistic and potentially misleading.

May/June 2010

92. According to the Principle of Conservatism, when should revenues or gains be recognised?
(A) As soon as a profitable contract is signed.
(B) When they are realised in the form of cash or legally enforceable debts.
(C) Whenever the market value of an asset increases.
(D) At the discretion of the company's management.

Ans :

(B) When they are realised in the form of cash or legally enforceable debts.
The principle of conservatism dictates a strict rule for revenue recognition. It states that revenues or gains should be recognised "only when they are realised in the form of cash or assets (usually legally enforceable debts), the ultimate cash realisation of which can be assessed with reasonable certainty." This prevents the recording of uncertain future gains.

Oct/Nov 2015

93. A company is facing a lawsuit from a customer. The outcome is uncertain, but the company's lawyers believe a loss is probable. According to the Principle of Prudence, what should the accountant do?
(A) Ignore the lawsuit until the court gives a final judgment.
(B) Disclose the lawsuit only if the company is certain to win.
(C) Provide for the likely loss in the financial statements.
(D) Record an asset representing the potential to win the case.

Ans :

(C) Provide for the likely loss in the financial statements.
This scenario represents a contingency with a probable loss. The chapter, in explaining conservatism, states that "Probable losses in respect of all contingencies should also be provided for." Therefore, the prudent action is to make a provision for the potential loss, reflecting a cautious approach and acknowledging the possible negative outcome.

May/June 2022

94. The application of the Principle of Conservatism is likely to result in which of the following outcomes?
(A) Overstated net assets and overstated income.
(B) Understated net assets and understated income.
(C) Perfectly accurate net assets and income.
(D) Overstated net assets and understated income.

Ans :

(B) Understated net assets and understated income.
The text explains the systematic bias introduced by conservatism. Because it advocates recording the lowest possible values for assets/revenues and the highest for liabilities/expenses, the chapter states that "net assets and income are likely to be understated rather than overstated." This cautious approach prioritizes avoiding overstatement of financial health.

Oct/Nov 2006

95. The widely advocated practice of valuing inventory at cost or market price, whichever is lower, is based on conservatism and in a way, modifies which other concept?
(A) The Cost Concept.

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(B) The Going Concern Concept
(C) The Business Entity Concept
(D) The Dual Aspect Concept

Ans :

(A) The Cost Concept.
The chapter notes that the "cost or market, whichever is lower" rule for inventory valuation is an application of conservatism. It then explicitly states, "You will note that this convention, in a way, modifies the earlier cost concept." While the cost concept dictates using historical cost, conservatism introduces an exception by requiring a write-down if the market value falls below cost.

May/June 2014

96. What is the recent criticism leveled against the Convention of Conservatism?
(A) It is considered too subjective and difficult for most professional accountants to apply in practice.
(B) It obstructs the fair determination of profit and a true and fair view of financial position.
(C) It consistently leads to a significant overstatement of reported profits and company assets.
(D) It is a fringe theory that is not recognized by any major professional accounting standards bodies.

Ans :

(B) It obstructs the fair determination of profit and a true and fair view of financial position.
The chapter mentions that the logic of conservatism has been under stress recently. "Many writers have challenged it on the ground that it stands in the way of fair determination of profit and the disclosure of the true and fair financial position of the business enterprise," as it can lead to a deliberate understatement of assets and profits.

Oct/Nov 2019

97. The saying "there is many a slip between the cup and the lip" is used to illustrate which accounting concept?
(A) The concept that revenue is recognized only when a sale is made.
(B) The concept that a business is separate from its owner.
(C) The concept that a business will continue for a long time.
(D) The concept that every transaction has a debit and a credit.

Ans :

(A) The concept that revenue is recognized only when a sale is made.
The section on Revenue Recognition and Realization begins with this saying. It is used to explain that merely acquiring something with the intent to sell at a profit is not enough to recognize that profit. The concept requires an actual sale to occur, where a legal obligation to pay is created, before revenue is recognized.

May/June 2008

98. The Revenue Recognition and Realization concept prevents business firms from doing what?
(A) Inflating their profits by recording expected incomes.
(B) Selling goods on credit.
(C) Paying dividends to shareholders.
(D) Investing in long-term assets.

Ans :

(A) Inflating their profits by recording expected incomes.
The chapter states that the revenue recognition concept "prevents business firms from inflating their profits by recording incomes that are likely to accrue, i.e. expected incomes or gains are not recorded." By requiring a realized sale, it ensures that reported profits are based on actual transactions, not on optimistic projections or expectations.

Oct/Nov 2024

99. What is the key distinction made by the Accrual Concept?
(A) The distinction between assets and liabilities.
(B) The distinction between profit and loss.
(C) The distinction between the receipt of cash and the right to receive it.
(D) The distinction between material and immaterial items.

Ans :

(C) The distinction between the receipt of cash and the right to receive it.
The Accrual Concept's core principle is the separation of the timing of cash flows from the recognition of revenues and expenses. The chapter explicitly states that it "makes a

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distinction between the receipt of cash and the right to receive it, and the payment of cash and the legal obligation to pay it."

May/June 2016

100. A company receives a cash advance in December for services it will provide in February of the next year. Under the accrual concept, how should this cash receipt be treated in December?

(A) It will not be recognized as revenue of the period.
(B) It should be recognized as revenue for the current period (December).
(C) It should be recorded as a miscellaneous expense.
(D) The transaction should be ignored until the service is performed.

Ans :

(A) It will not be recognized as revenue of the period.
This scenario is described as revenue being received "before the right to receive arises." The chapter explains that in this case, "the receipt will not be recognized as the revenue of the period for the reason that the right to receive the same has not yet arisen." It is treated as a liability (unearned revenue) until earned.

Oct/Nov 2011

101. A company incurs electricity expenses for the month of March but receives the bill and pays it in April. According to the accrual concept, when should this expense be recorded?

(A) In April, when the cash is paid.
(B) It should be split equally between March and April.
(C) It should not be recorded as an expense, but as a loss.
(D) It must be recorded as an expense in March.

Ans :

(D) It must be recorded as an expense in March.
This illustrates an expense incurred but not yet paid. The accrual concept dictates that the expense belongs to the period in which the benefit was received (electricity used in March). The text states, "Where an expense has been incurred during the accounting period but no payment has been made, the expense must be recorded."

May/June 2020

102. Which of the following is an essential feature of the accrual concept?

(A) Revenue is recognised only when cash is received.
(B) Costs are matched against revenues on the basis of the relevant time period.
(C) All costs are charged to income in the period they are paid.
(D) Costs that have lost their utility are carried forward as assets indefinitely.

Ans :

(B) Costs are matched against revenues on the basis of the relevant time period.
The chapter lists three essential features of the accrual concept. The second feature is that "Costs are matched against revenues on the basis of the relevant time period to determine periodic income." This directly relates to the matching principle, which is a cornerstone of accrual accounting, linking it to revenue earned in the same period.

Oct/Nov 2016

103. According to standard accounting principles, an entity shall prepare its financial statements using the accrual basis of accounting, with one exception. What is that exception?

(A) The Balance Sheet.
(B) The Profit and Loss Statement.
(C) Cash flow information.
(D) Notes to the Accounts.

Ans :

(C) Cash flow information.
The quote from Ind AS-1 is precise: "An entity shall prepare its financial statements, except for cash flow information, using the accrual basis of accounting." The cash flow statement is, by its very nature, prepared on a cash basis, as its purpose is to show the movement of cash and cash equivalents.

May/June 2007

104. According to standard accounting principles, under the accrual basis, an entity recognises items like assets and liabilities when they satisfy the definitions and what other criteria?

(A) The materiality criteria for the transaction, as judged by the senior management team.
(B) The consistency criteria, ensuring the same treatment is applied as in previous accounting

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periods.
(C) The specific internal criteria for recognition as set forth by the company's own board of directors.
(D) The recognition criteria for those elements in the conceptual framework.

Ans :

(D) The recognition criteria for those elements in the conceptual framework.
The quote from Ind AS-1 states that items are recognized "when they satisfy the definitions and recognition criteria for those elements in the conceptual framework." This means an item must not only meet the definition of an asset, liability, etc., but also meet the specific conditions for being formally recorded in the financial statements.

Oct/Nov 2021

105. Consider the following statements regarding the Accrual Concept:
1. Revenue is recognised when it is earned, not when cash is received.
2. Costs are charged to income when they are paid in cash.
3. Costs that have lost their power to generate future revenue are written off as a loss.

Which of the above statements are correct?
(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(C) 1 and 3 only.
Statement 1 is a core principle of accrual accounting. Statement 3 is also correct, as costs that no longer provide future benefits are expensed or written off. Statement 2 is incorrect; under the accrual concept, costs are matched with revenues in the period they are incurred, not necessarily when they are paid in cash.

May/June 2012

106. What is the primary function of the rules and conventions known as 'Generally Accepted Accounting Principles' (GAAP)?
(A) To provide guidelines for preparing, maintaining, and recording business transactions.
(B) To directly dictate and control the stock market price of a public company's shares.
(C) To prescribe specific, mandatory business strategies for achieving maximum profitability.
(D) To ensure all businesses, regardless of size or industry, use the same standardized accounting software.

Ans :

(A) To provide guidelines for preparing, maintaining, and recording business transactions.
The "Let Us Sum Up" section summarizes that to achieve accounting objectives, a systematic record is maintained. It states, "There are certain rules and regulations that are used as guidelines to prepare, maintain and record all business transactions in the form of accounting books." These are known as GAAP or Basic Accounting Concepts.

Oct/Nov 2009

107. Match List-I (Accounting Concept) with List-II (Core Principle).
List-I
P. Business Entity
Q. Going Concern
R. Money Measurement
S. Cost Concept
List-II
1. Record transactions at original purchase price.
2. Only transactions expressible in money are recorded.
3. Business is distinct from its owner.
4. Business will operate for the foreseeable future.

(A) P-3, Q-4, R-2, S-1
(B) P-4, Q-3, R-1, S-2
(C) P-3, Q-2, R-4, S-1
(D) P-1, Q-4, R-2, S-3

Ans :

(A) P-3, Q-4, R-2, S-1
P (Business Entity) matches with 3 (Business is distinct from its owner). Q (Going Concern) matches with 4 (Business will operate for the foreseeable future). R (Money Measurement) matches with 2 (Only transactions expressible in money are recorded). S (Cost Concept) matches with 1 (Record transactions at original purchase price).

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May/June 2023

108. According to the classification of concepts, which of the following pairs of concepts are both classified under the 'Reporting Stage'?

(A) Going concern concept and Convention of Consistency.
(B) Cost concept and Matching concept
(C) Business entity concept and Convention of Full disclosure
(D) Realization concept and Dual aspect concept

Ans :

(A) Going concern concept and Convention of Consistency.
The standard classification of accounting concepts lists both the 'Going concern concept' and the 'Convention of Consistency' under the heading 'At the Reporting Stage'. The other options contain a mix of concepts from both the recording and reporting stages, making them incorrect pairings for this specific category.

Oct/Nov 2018

109. Based on the listed applications of the cost concept, which of the following statements is correct?

(A) Fixed assets are to be shown at their current market value.
(B) Future values are preferred over present values for recording transactions.
(C) An item acquired without any cost is not recorded in the books.
(D) Unrealised gains from holding assets should be recognized and recorded.

Ans :

(C) An item acquired without any cost is not recorded in the books.
The applications for the Cost Concept explicitly include the rule that "An item, that has no cost, is not taken in books." The other options contradict the listed applications, which state that fixed assets are kept at cost, present values are used, and unrealised gains are ignored.

May/June 2019

110. Based on the typical description of the single-entry system, which statement accurately describes it?

(A) It is unreliable because the accounts it maintains are incomplete and unsystematic.
(B) It is a highly scientific and reliable system mandated for use by most large business houses.
(C) Under this system, nominal and real accounts are maintained with meticulous detail and accuracy.
(D) It is based on the rigorous dual aspect analysis, recording two effects for every transaction.

Ans :

(A) It is unreliable because the accounts it maintains are incomplete and unsystematic.
The single-entry system is described as "unscientific" and the accounts maintained under it are "incomplete and unsystematic and, therefore, the system is not reliable." It is typically used by small firms, does not maintain full nominal and real accounts, and is not based on the dual aspect concept.

Oct/Nov 2025

111. Which of the following is typically listed as a merit of the Double Entry System?

(A) It is known as the simplest and least time-consuming accounting system to maintain.
(B) It guarantees the prevention of all types of fraud.
(C) It requires only minimal record-keeping effort, focusing primarily on cash transactions.
(D) It enables a businessman to control his business activities through comparison with previous years.

Ans :

(D) It enables a businessman to control his business activities through comparison with previous years.
One of the key merits of the Double Entry System is that it allows for the comparison of current year figures with previous years, "thus enabling a businessman to control his business activities." While it helps detect fraud, it doesn't guarantee prevention. It is more complex and requires more effort than the single-entry system.

May/June 2011

112. The applications of the Convention of Conservatism include several practices. Which of the following would be a violation of this convention?

(A) Creating a provision for doubtful debts.
(B) Valuing the stock in hand at the higher of cost or market value.

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(C) Creating a contingency reserve.
(D) Showing a joint life policy at its surrender value.

Ans :

(B) Valuing the stock in hand at the higher of cost or market value.
A key application of conservatism is to "Value the stock in hand at lower of the cost or market value." Choosing the higher value would recognize an unrealized gain if the market value is higher than cost, which directly violates the principle of conservatism or prudence.

Oct/Nov 2010

113. The highly skilled and innovative research team of a pharmaceutical company is considered its most valuable asset by industry experts. However, the company's accountant does not assign a value to this team on the balance sheet. This accounting treatment is a direct consequence of which concept?
(A) The Going Concern Concept
(B) The Money Measurement Concept
(C) The Conservatism Concept
(D) The Business Entity Concept

Ans :

(B) The Money Measurement Concept.
The Money Measurement Concept restricts accounting records to only those items that can be expressed in monetary terms. While the research team is undoubtedly valuable, its worth cannot be objectively quantified in money. Therefore, just like the health of a manager, this vital but non-monetary 'asset' is excluded from the financial statements.

May/June 2017

114. Which of the following describes the most significant difference between the single entry and double entry systems of bookkeeping?
(A) The single entry system is used for manufacturing firms, while double entry is exclusively for service firms.
(B) The single entry system only uses a debit column, while double entry uses both debit and credit columns.
(C) The double entry system records both aspects of a transaction, whereas the single entry system does not.
(D) The single entry system is a fully computerized system, while the double entry system is a purely manual one.

Ans :

(C) The double entry system records both aspects of a transaction, whereas the single entry system does not.
The fundamental difference highlighted in the chapter is the application of the dual aspect concept. The double entry system is built upon recording the two aspects (debit and credit) of every transaction. In contrast, the single entry system is described as unscientific because it fails to do this, recording some transactions partially and others not at all.

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Oct/Nov 2022

115. Which accounting concept is primarily responsible for the practice of preparing financial statements for a specific period, such as a year, even though the business is expected to continue indefinitely?
(A) Accounting Period Concept.
(B) Money Measurement Concept
(C) Historical Records Concept
(D) Dual Aspect Concept

Ans :

(A) Accounting Period Concept.
The Accounting Period Concept addresses the conflict between the Going Concern assumption (indefinite life) and the need for periodic performance evaluation. It mandates breaking the continuous life of a business into shorter, artificial time periods (like a year) for the purpose of preparing financial statements and reporting results to stakeholders.

May/June 2013

116. Identify the incorrect statement regarding accounting conventions.
(A) They are generally accepted customs and traditions used as a guide for preparing accounting standards.
(B) The convention of conservatism suggests anticipating all profits and providing for known losses.
(C) The convention of full disclosure requires that all information material to a user's decision must be revealed.
(D) The convention of consistency is designed to promote the comparability of financial statements across periods.

Ans :

(B) The convention of conservatism suggests anticipating all profits and providing for known losses.

This statement misrepresents the convention of conservatism. The principle is "anticipate no profit, provide for all possible losses." It specifically forbids the anticipation of profits. The other statements accurately describe the nature of conventions, the principle of full disclosure, and the goal of consistency as explained in the chapter.

Oct/Nov 2005

117. If an accountant treats the purchase of a wastepaper basket as an expense rather than an asset, the decision is most likely guided by a trade-off between which two conventions/concepts?

(A) Going Concern and Full Disclosure
(B) Cost Concept and Materiality
(C) Business Entity and Consistency
(D) Realisation and Conservatism

Ans :

(B) Cost Concept and Materiality.

Theoretically, under the cost concept, the wastepaper basket is an asset. However, its value is insignificant. The materiality convention allows the accountant to disregard the strict theoretical treatment because the cost of tracking it as an asset outweighs the benefit. The accountant thus applies materiality to override the strict application of the cost concept for trivial items.

May/June 2024

118. Which of the following pairs of concepts is incorrectly matched?

(A) Dual Aspect Concept : Assets = Capital + Liability
(B) Business Entity Concept : Owner is not distinct from the business
(C) Conservatism Concept : Value stock at lower of cost or market value
(D) Money Measurement Concept : Ignore non-monetary transactions

Ans :

(B) Business Entity Concept : Owner is not distinct from the business.

The Business Entity Concept's fundamental principle is that the business is considered separate and distinct from its owner for accounting purposes. The matched description is the exact opposite of the concept's meaning. The other pairs are correctly matched according to the principles and applications described in the chapter.

Oct/Nov 2008

119. Consider the following actions:

1. Creating a provision for warranty claims.
2. Valuing investments at market price even if it is higher than cost.
3. Deferring recognition of revenue until cash is received.
4. Expensing a small calculator in the year of purchase.

Which of these actions are consistent with the Principle of Conservatism?

(A) 1 and 4 only
(B) 1 and 3 only
(C) 2 and 4 only
(D) 1, 3 and 4

Ans :

(B) 1 and 3 only.

Creating a provision for warranty claims (1) is providing for a possible loss. Deferring revenue recognition until cash is received (3) is a highly cautious approach to recognizing gains. Both are conservative actions. Valuing investments at a higher market price (2) recognizes an unrealized gain, violating conservatism. Expensing a calculator (4) is an application of materiality, not conservatism.

May/June 2006

120. **Assertion (A) :** Financial statements are prepared on a specific date or for a specific period.
Reason (R) : The Accounting Period Concept assumes that the life of a business can be divided into shorter intervals for performance measurement.

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).

Assertion (A) is a fact about financial reporting. Reason (R) correctly states the essence of the

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Accounting Period Concept. The reason (R) directly explains why financial statements are prepared for specific periods (A), as this concept provides the conceptual justification for breaking down the continuous life of a business for reporting purposes.

Oct/Nov 2017

121. Which accounting principle primarily governs the timing of revenue recognition?
(A) Cost Concept
(B) Matching Concept
(C) Realization Concept
(D) Materiality Concept

Ans :

(C) Realisation Concept.
The Realization Concept specifically addresses the question of when revenue should be considered earned and recorded in the books. It sets the criterion that revenue is realised when the property in goods passes to the buyer, and they become legally liable to pay, thus determining the timing of revenue entry.

May/June 2009

122. Which of the following statements correctly differentiates between accounting concepts and conventions?
(A) Concepts are legally binding and enforced by law, whereas all accounting conventions are entirely optional.
(B) Concepts are basic assumptions, while conventions are customs that guide the preparation of standards.
(C) Concepts apply only to the valuation and recording of assets, whereas conventions apply only to liabilities.
(D) Concepts are primarily used for internal management reporting, whereas conventions are used for external financial reporting.

Ans :

(B) Concepts are basic assumptions, while conventions are customs that guide the preparation of standards.
The chapter distinguishes between the two, stating that concepts are the "basic assumptions or conditions on which the service of accounting is based," while conventions "denote customs and traditions that have been accepted as a guide for the preparation of the accounting standards." This reflects their different roles in the accounting framework.

Oct/Nov 2013

123. The argument that the cost concept meets the criteria of relevance, objectivity, and feasibility supports its use over which alternative valuation method?
(A) Liquidation value
(B) Market value
(C) Future value
(D) Replacement value

Ans :

(B) Market value.
The discussion compares the historical cost basis with the alternative of using current market values. The chapter notes that assets are sometimes shown at cost even when market values are widely different. The argument for using cost is that it is relevant, objectively verifiable from past transactions, and feasible to implement, unlike market values which can be subjective and volatile.

May/June 2015

124. Which concept ensures that personal assets and liabilities of a business owner are not mixed with the assets and liabilities of the business in its financial statements?
(A) Going Concern Concept
(B) Business Entity Concept
(C) Matching Concept
(D) Conservatism Concept

Ans :

(B) Business Entity Concept.
The Business Entity Concept mandates the separation of the business from its owner. This implies that the owner's personal financial affairs, including personal assets and obligations (like mortgages, personal debts), will not appear in the business's books of account, ensuring the financial statements reflect only the business's position and performance.

Oct/Nov 2023

125. Which of the following is a key reason for adopting a 'natural business year' for accounting?
(A) It perfectly aligns with the government's fiscal year, thereby simplifying corporate tax filing.
(B) Business activity is at its lowest point, which

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simplifies year-end accounting procedures.
(C) It is the only acceptable accounting period allowed under International Financial Reporting Standards (IFRS).
(D) It is a method specifically designed to maximize the reported profit for any given accounting year.

Ans :

(B) Business activity is at its lowest point, which simplifies year-end accounting procedures.
The chapter defines the 'natural business year' as a twelve-month period where the end "is marked by the relatively lower or lowest volume of business activity." This timing is advantageous for tasks like inventory counting and closing the books, as business operations are at a lull, allowing for greater accuracy and less disruption.

May/June 2021

126. Match List-I (Accounting Convention) with List-II (Application).
List-I
P. Conservatism
Q. Consistency
R. Full Disclosure
S. Materiality
List-II
1. Appending notes for contingent liabilities.
2. Expensing a low-cost asset in the year of purchase.
3. Continuing to use the same depreciation method.
4. Creating a provision for doubtful debts.
(A) P-4, Q-3, R-1, S-2
(B) P-3, Q-4, R-2, S-1
(C) P-4, Q-1, R-3, S-2
(D) P-2, Q-3, R-1, S-4

Ans :

(A) P-4, Q-3, R-1, S-2
P (Conservatism) is applied by creating provisions for doubtful debts (4). Q (Consistency) is applied by using the same depreciation method year after year (3). R (Full Disclosure) is applied by reporting contingent liabilities in notes (1). S (Materiality) is applied by expensing a low-cost asset immediately (2).

Oct/Nov 2014

127. What is the ultimate effect of the Double Entry System on the accounting equation?
(A) It causes the fundamental accounting equation to be in a constant and unresolvable state of imbalance.
(B) It ensures the equation Assets = Capital + Liability stays balanced after every transaction.
(C) It is a specialized system that applies only to the asset side of the fundamental accounting equation.
(D) It requires the fundamental accounting equation to be checked for balance only once at the end of the year.

Ans :

(B) It ensures the equation Assets = Capital + Liability stays balanced after every transaction.
The double entry system is based on the dual aspect concept, where every transaction has equal debit and credit effects. This mechanism inherently ensures that the fundamental accounting equation, Assets = Capital + Liability, remains balanced after each and every transaction is recorded, maintaining the integrity of the financial records at all times.

May/June 2005

128. Which of the following four statements about basic accounting procedures are correct?
1. The Realisation concept states that revenue is earned when cash is received.
2. The Historical Records concept involves recording transactions as and when they take place.
3. The Single Entry system is considered scientific and is used by most large businesses.
4. The Matching concept's justification arises from the Accounting Period concept.
(A) 1 and 3 only
(B) 2 and 4 only
(C) 1, 2 and 4
(D) 2, 3 and 4

Ans :

(B) 2 and 4 only.
Statement 2 is correct as the historical record concept is about recording past events chronologically. Statement 4 is correct as stated in the text. Statement 1 is incorrect; realisation is tied to the transfer of property and legal obligation, not cash receipt. Statement 3 is incorrect; single entry is unscientific and used by small firms.

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Oct/Nov 2020

129. An accountant's decision to ignore the impact of inflation on the value of a company's assets is a direct consequence of which concept?

(A) The Going Concern Concept
(B) The Money Measurement Concept
(C) The Conservatism Concept
(D) The Full Disclosure Concept

Ans :

(B) The Money Measurement Concept.
The chapter discusses the limitations of the Money Measurement Concept, highlighting its assumption of a stable monetary unit. This assumption means that subsequent changes in the purchasing power of money (inflation or deflation) are ignored in the primary accounting records, and asset values are not adjusted for such changes.

May/June 2018

130. Which of the following practices is NOT a merit of the Double Entry System?

(A) Preparation of a detailed profit and loss account is possible.
(B) It allows for the easy detection and commission of fraud.
(C) It keeps a complete record of both personal and impersonal accounts.
(D) A balance sheet showing assets, liabilities, and capital can be prepared.

Ans :

(B) It allows for the easy detection and commission of fraud.
The statement is contradictory. The chapter lists as a merit that the system, being scientific, "prevents commission of fraud and, if a fraud is committed, it can be easily detected." The cross-checking nature of debits and credits makes it harder to commit fraud and easier to detect, not the other way around.

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CHAPTER 3

Maintenance of Cash/Subsidiary Books and Ledger

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May/June 2017

1. According to the fundamental principle of the 'Double Entry Book Keeping' system, what is the effect of every business transaction?

(A) It affects only one account, which is either debited or credited, a practice found in single-entry bookkeeping systems.

(B) It has a two-fold financial aspect, affecting two accounts, one debited and the other credited with a like amount.

(C) It affects multiple accounts, with the total debits not necessarily equalling the total credits, which violates the core principle.

(D) It only impacts the financial position through a single entry, without requiring a corresponding debit and credit in the books.

Ans :

(B) It has a two-fold financial aspect, affecting two accounts, one debited and the other credited with a like amount.

The Double Entry Book Keeping system is based on the core principle that every transaction has two aspects. This means for every debit entry in one account, there must be a corresponding credit entry of an equal amount in another account, ensuring the accounting equation remains balanced and providing a complete record of the transaction's financial impact.

Oct/Nov 2024

2. Bookkeeping is defined as the art of recording business transactions with a view to having a permanent record and showing their effect on what?

(A) Wealth

(B) Employee morale

(C) Market share

(D) Production efficiency

Ans :

(A) Wealth

Bookkeeping serves as the systematic recording of pecuniary transactions, which are those involving money or money's worth. The primary objective of this process is to create a permanent record of these transactions and to clearly demonstrate their cumulative effect on the business's overall wealth, financial position, and performance over a specific period of time.

May/June 2009

3. Which of the following is NOT one of the key pieces of information a trader can ascertain from properly maintained books of accounts?

(A) The nature and value of assets and amounts owed by sundry debtors.

(B) The amount of liabilities and amounts owed to sundry creditors.

(C) The marketing strategies of key competitors.

(D) Whether a profit or loss has been made during a given period.

Ans :

(C) The marketing strategies of key competitors.

Bookkeeping focuses on recording and summarizing a firm's own financial transactions. It helps ascertain assets, liabilities, profit or loss, and solvency. Information about competitors' marketing strategies falls outside the scope of internal accounting records and is typically gathered through market intelligence, not through the bookkeeping process which is internally focused on the entity's own financial data.

Oct/Nov 2011

4. What is the primary characteristic of a journal in the accounting process?

(A) It is an analytical record of all transactions, sorted by account type.

(B) It is the final book of entry where account balances are summarized.

(C) It contains only cash transactions and serves as the cash account.

(D) It is a chronological record of all transactions, showing the debit and credit aspects.

Ans :

(D) It is a chronological record of all transactions, showing the debit and credit aspects.
The journal is the book of primary or original entry where transactions are first recorded in the order they occur. It provides a chronological, day-to-day history of all business dealings. Each entry in the journal specifies the accounts to be debited and credited, along with a narrative description, forming the basis for posting to the ledger.

May/June 2010

5. What purpose does the Ledger Folio (L.F.) column in a journal serve?
(A) It contains a narrative description of the transaction.
(B) It records the date of the transaction.
(C) It indicates the page number in the ledger where the entry is posted.
(D) It records the serial number of the journal entry.

Ans :

(C) It indicates the page number in the ledger where the entry is posted.
The Ledger Folio (L.F.) column acts as a cross-reference between the journal and the ledger. When a journal entry is transferred, or 'posted', to the respective accounts in the ledger, the page number of that ledger account is recorded in the L.F. column of the journal. This linkage facilitates easy tracking and verification of entries between the two books.

Oct/Nov 2005

6. Why is a cash book considered both a subsidiary book and a ledger account?
(A) Because it only records credit transactions and summarizes them at the end of the period.
(B) Because it serves as a book of original entry for cash transactions and also functions as the cash account itself.
(C) Because it records all transactions chronologically and analytically at the same time.
(D) Because it is prepared after the trial balance to verify cash balances.

Ans :

(B) Because it serves as a book of original entry for cash transactions and also functions as the cash account itself.
The cash book is unique in its dual role. It is a subsidiary book (or book of original entry) because all cash transactions are first recorded in it. It is also a ledger account because it is maintained in the format of an account, with debit and credit sides, thereby eliminating the need for a separate cash account in the ledger.

May/June 2020

7. In a cash book, on which side are all cash receipts and cash payments recorded?
(A) Receipts on the credit side and payments on the debit side.
(B) Both receipts and payments on the debit side.
(C) Both receipts and payments on the credit side.
(D) Receipts on the debit side and payments on the credit side.

Ans :

(D) Receipts on the debit side and payments on the credit side.
The cash book follows the rule of a real account, specifically the cash account. The rule is "Debit what comes in, Credit what goes out." Therefore, all cash inflows or receipts are recorded on the debit (Dr.) side, representing an increase in cash. All cash outflows or payments are recorded on the credit (Cr.) side, representing a decrease in cash.

Oct/Nov 2015

8. What are the three stages of the accounting cycle in their correct sequence?
(A) Recording, Classifying, Summarising
(B) Summarising, Recording, Classifying
(C) Classifying, Recording, Summarising
(D) Recording, Summarising, Classifying

Ans :

(A) Recording, Classifying, Summarising
The accounting cycle follows a logical sequence. First is 'Recording,' where transactions are entered into a journal or subsidiary books. Second is 'Classifying,' where these entries are posted to their respective ledger accounts. The final stage is 'Summarising,' which involves preparing the trial balance and final accounts to ascertain the financial position and performance of the business.

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May/June 2013

9. What is the main function of a ledger?
(A) To record transactions chronologically as they occur.
(B) To provide a narrative description for every business transaction.
(C) To classify and sort all items from the journal into their appropriate accounts.
(D) To serve as documentary evidence for cash payments made by the business.

Ans :

(C) To classify and sort all items from the journal into their appropriate accounts.
The ledger is the principal book of accounts, and its primary function is classification. It groups all transactions related to a particular person, asset, liability, income, or expense into one place, known as an account. This sorting process allows the business to see the combined effect of all transactions on each individual account and for the entire enterprise.

Oct/Nov 2021

10. In a standard ledger account format, what does the abbreviation 'J.F.' stand for?
(A) Journal Folio
(B) Justified Figure
(C) Joint Finance
(D) Journalised Form

Ans :

(A) Journal Folio
In a ledger account, the 'J.F.' column stands for Journal Folio. This column is used to record the page number of the journal from which the entry has been posted. It serves as a cross-reference, linking the entry in the ledger account back to its original, chronological record in the journal, which is essential for auditing and verification purposes.

May/June 2024

11. Which statement correctly describes the relationship between a journal and a ledger?
(A) The ledger is the book of original entry, and the journal is the book of second entry.
(B) The journal is a book for analytical record, while the ledger is for chronological record.
(C) The process of recording in the journal is called 'posting', and in the ledger, it is called 'journalising'.
(D) Transactions are recorded first in the journal and then posted to the ledger.

Ans :

(D) Transactions are recorded first in the journal and then posted to the ledger.
The journal is the book of first or original entry, where transactions are recorded chronologically. The ledger is the book of second entry, where these transactions are classified and summarized by account. The process involves recording entries in the journal first and then transferring, or 'posting', them to the appropriate accounts in the ledger for analytical purposes.

Oct/Nov 2008

12. The process of transferring debit and credit items from the journal to their respective accounts in the ledger is known as what?
(A) Journalizing
(B) Posting
(C) Balancing
(D) Summa rising

Ans :

(B) Posting
'Posting' is the specific term used to describe the process of transferring entries from the journal, the book of original entry, to the ledger, the principal book of accounts. This systematic transfer ensures that all transactions affecting a particular account are brought together under one head, facilitating the classification stage of the accounting cycle before summarizing.

May/June 2006

13. When posting a debit entry from the journal to a ledger account, which convention is customarily followed?
(A) The word 'By' is used with the account name on the debit side.
(B) The word 'To' is used with the account name on the credit side.
(C) The word 'To' is used with the name of the other account that was credited in the journal entry.
(D) No prefix is used; only the account name is written.

Ans :

(C) The word 'To' is used with the name of the other account that was credited in the journal entry.

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It is a customary practice in ledger posting to use the word 'To' before the name of the account on the debit side of an account. This 'To' is followed by the name of the account that was credited in the corresponding journal entry, thereby completing the double-entry record within the ledger itself and indicating the source of the debit.

Oct/Nov 2017

14. What does it mean when a ledger account is said to have a 'debit balance'?

(A) The total of the credit side is greater than the total of the debit side.
(B) The total of the debit side is equal to the total of the credit side.
(C) The account has been permanently closed and transferred to the profit and loss account.
(D) The total of the debit side is greater than the total of the credit side.

Ans :

(D) The total of the debit side is greater than the total of the credit side.
A debit balance arises in an account when the sum of all debit entries exceeds the sum of all credit entries. To equalize the two sides for balancing, the difference is placed on the credit side as 'By Balance c/d'. This balance is then brought down to the debit side for the next accounting period, reflecting its nature as a debit balance.

May/June 2008

15. If the credit side total of an account is more than the debit side total, how is the account balanced?

(A) The difference is put on the debit side by writing 'To Balance c/d'.
(B) The difference is put on the credit side by writing 'By Balance c/d'.
(C) The account is simply closed without carrying down any balance.
(D) The difference is put on the debit side by writing 'To Balance b/d'.

Ans :

(A) The difference is put on the debit side by writing 'To Balance c/d'.
When the credit side total exceeds the debit side total, the account has a credit balance. To balance the account, the difference (the credit balance) is entered on the debit side with the description 'To Balance c/d' (carried down). This equalizes the totals. The same amount is then brought down to the credit side as 'By Balance b/d'.

Oct/Nov 2013

16. A debit balance in a Personal Account typically represents what?

(A) A creditor, i.e., an amount owed by the business.
(B) A debtor, i.e., an amount owed to the business.
(C) A business expense.
(D) A business income.

Ans :

(B) A debtor, i.e., an amount owed to the business.
In a Personal Account, a debit balance signifies that the person or entity owes money to the business. The person has received benefits (like goods or services on credit) from the business without having paid for them yet. Therefore, such an account represents a debtor, which is an asset for the business, reflecting a future economic benefit.

May/June 2015

17. What does a credit balance in a Nominal Account represent?

(A) A gain or an income.
(B) An expense or a loss.
(C) A property or an asset.
(D) A liability or a creditor.

Ans :

(A) A gain or an income.
Nominal accounts relate to incomes, gains, expenses, and losses. According to the rules of accounting, all incomes and gains are credited. Therefore, a credit balance in a nominal account, such as Sales Account or Commission Received Account, represents a gain or income earned by the business during the accounting period, increasing the business's profit.

Oct/Nov 2012

18. At the end of an accounting year, what happens to the balances of Nominal Accounts?

(A) They are transferred to the 'Trading and Profit and Loss Account'.
(B) They are carried down to the next year as opening balances.
(C) They are transferred to the Balance Sheet as assets or liabilities.
(D) They are ignored and reset to zero without any transfer entry.

Ans :

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(A) They are transferred to the 'Trading and Profit and Loss Account'.
Nominal accounts are temporary accounts used to track incomes and expenses for a specific period. At the end of the accounting year, their balances are not carried forward. Instead, they are closed by transferring them to the Trading and Profit and Loss Account to calculate the net profit or loss for that particular period.

May/June 2011

19. On Jan 1, 2022, a business purchases goods on credit from Ashoka for ₹5,000. On Jan 18, a payment of ₹4,000 is made to Ashoka. How would Ashoka's account appear after these two transactions are posted?
(A) A debit of ₹4,000 and a credit of ₹5,000, resulting in a ₹1,000 debit balance.
(B) A debit of ₹5,000 and a credit of ₹4,000, resulting in a ₹1,000 debit balance.
(C) A debit of ₹4,000 and a credit of ₹5,000, resulting in a ₹1,000 credit balance.
(D) A debit of ₹5,000 and a credit of ₹4,000, resulting in a ₹1,000 credit balance.

Ans :

(C) A debit of ₹4,000 and a credit of ₹5,000, resulting in a ₹1,000 credit balance.
The purchase on credit makes Ashoka a creditor (giver), so Ashoka's account is credited with ₹5,000. The cash payment makes Ashoka the receiver, so Ashoka's account is debited with ₹4,000. The credit side (₹5,000) is greater than the debit side (₹4,000), resulting in a credit balance of ₹1,000, which represents the amount still owed to Ashoka.

Oct/Nov 2020

20. A business sells goods to Madhav on credit for ₹4,000 on Jan 6 and receives ₹2,000 from him on account on Jan 20. What is the final status of Madhav's account?
(A) It shows a debit balance of ₹2,000.
(B) It shows a credit balance of ₹2,000.
(C) It shows a debit balance of ₹4,000.
(D) It is balanced with no outstanding amount.

Ans :

(A) It shows a debit balance of ₹2,000.
When goods are sold on credit to Madhav, he becomes the receiver and hence a debtor. His account is debited with ₹4,000. When cash is received from him, he becomes the giver, and his account is credited with ₹2,000. The debit total (₹4,000) exceeds the credit total (₹2,000), leaving a debit balance of ₹2,000, representing the amount still receivable from Madhav.

May/June 2022

21. According to Kohler's Dictionary for Accountants, an account is defined as a formal record of a particular type of transaction expressed in what terms?
(A) Units of production
(B) Customer satisfaction
(C) Percentage of market share
(D) Terms of money

Ans :

(D) Terms of money
An account is a fundamental component of the accounting system. As defined, it is a formal, structured record used to accumulate and summarize the effects of transactions on a specific item like an asset, liability, equity, revenue, or expense. A key characteristic is that all these transactions are expressed in a common denominator, which is monetary terms.

Oct/Nov 2023

22. Accounts are broadly classified into which two primary classes?
(A) Real Accounts and Nominal Accounts
(B) Personal Accounts and Impersonal Accounts
(C) Debit Accounts and Credit Accounts
(D) Asset Accounts and Liability Accounts

Ans :

(B) Personal Accounts and Impersonal Accounts
The initial broad classification of accounts divides them into two main categories. Personal Accounts relate to persons and institutions. Impersonal Accounts relate to all other items. The Impersonal Accounts category is then further subdivided into Real Accounts (relating to assets and properties) and Nominal Accounts (relating to incomes, expenses, gains, and losses).

May/June 2016

23. Which of the following is an example of an Artificial Personal Account?
(A) Mohan's account
(B) Proprietor's capital account
(C) Any limited company's account
(D) Salary outstanding account

Ans :

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(C) Any limited company's account
Artificial Personal Accounts are accounts of corporate bodies or institutions that are recognized as persons in business dealings, though they do not have a physical existence like natural persons. A limited company, a bank, or a club are created by law and are considered separate legal entities, hence their accounts fall under this category.

Oct/Nov 2009

24. A 'Rent Outstanding Account' is classified as what type of account?
(A) Nominal Account
(B) Real Account
(C) Artificial Personal Account
(D) Representative Personal Account

Ans :

(D) Representative Personal Account
A 'Rent Outstanding Account' represents the amount of rent due to one or more property owners (persons). Since it represents a person or a group of persons to whom money is owed, it is classified as a Representative Personal Account. It represents the landlord(s) who are creditors of the business for the amount of rent outstanding.

May/June 2023

25. Which of the following is an example of an Intangible Real Account?
(A) Land and building
(B) Cash in hand
(C) Goodwill
(D) Furniture

Ans :

(C) Goodwill
Real accounts pertain to assets or properties. They are divided into tangible and intangible. Tangible real assets, like buildings or cash, have a physical existence. Intangible real assets, such as goodwill, trademarks, and patent rights, lack physical substance but possess monetary value and can be measured in terms of money, representing valuable rights or advantages.

Oct/Nov 2018

26. Why are accounts like Salary, Rent, and Wages classified as Nominal Accounts?
(A) Because they represent the various tangible assets that are owned and utilized by the business.
(B) To explain the nature of financial transactions such as expenses, losses, incomes, and gains.
(C) Because they represent specific persons or entities to whom the business owes money or is owed money from.
(D) Because they represent items that can be physically touched, seen, and counted, such as inventory or cash.

Ans :

(B) To explain the nature of financial transactions such as expenses, losses, incomes, and gains.
Nominal accounts do not have a physical existence in themselves. They are created to classify and explain the nature of financial transactions. When salary is paid, cash (a real account) goes out. The 'Salary Account' is opened as a nominal account to explain why the cash was spent, categorizing it as a business expense.

May/June 2007

27. Identify the correct pair from the following options.
(A) Bank Loan Account - Real Account
(B) Trademarks Account - Personal Account
(C) Investment Account - Nominal Account
(D) Rent Outstanding Account - Representative Personal Account

Ans :

(D) Rent Outstanding Account - Representative Personal Account
A Rent Outstanding Account represents the amount payable to landlords, who are persons. Thus, it is a Representative Personal Account. Bank Loan is an Artificial Personal Account (representing the bank). Trademarks are Intangible Real Accounts. Investment is a Real Account. Therefore, the only correctly matched pair is the Rent Outstanding Account.

Oct/Nov 2025

28. Which of the following accounts would be classified as a Real Account?
(A) Stock in Hand Account
(B) Salaries Account
(C) Tata Iron & Steel Co. Account
(D) Commission Received Account

Ans :

(A) Stock in Hand Account
Real Accounts relate to the properties and assets of a business. Stock in hand represents the goods

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owned by the business at a particular point in time, which is a tangible asset. Salaries and Commission Received are Nominal Accounts (expense and income, respectively). Tata Iron & Steel Co. is an Artificial Personal Account.

May/June 2012

29. The account of a proprietor, such as 'Rajesh - Capital', falls under which category?
(A) Artificial Personal Account
(B) Representative Personal Account
(C) Natural Personal Account
(D) Nominal Account

Ans :

(C) Natural Personal Account
Natural Personal Accounts are accounts of human beings, who are creations of God. The proprietor of a business (e.g., Rajesh) is an individual. The capital account represents the proprietor's investment in the business and all transactions with him. Therefore, it is classified as a Natural Personal Account, representing the owner as a person.

Oct/Nov 2014

30. Which of the following is NOT a Personal Account?
(A) Bills receivable account
(B) Bank account
(C) Santosh's account
(D) Capital account

Ans :

(A) Bills receivable account
A Bank account is an Artificial Personal Account. Santosh's account is a Natural Personal Account. A Capital account is a Natural Personal Account (representing the owner). A Bills Receivable account represents a document that is an asset of the business, a promise to receive money. It is therefore classified as a Real Account, not a Personal Account.

May/June 2019

31. The act of recording an entry on the left side of an account is called:
(A) Crediting the account
(B) Balancing the account
(C) Posting the account
(D) Debiting the account

Ans :

(D) Debiting the account
By convention, the left side of any T-account is designated as the debit side, and the right side is the credit side. The process of making an entry on this left, or debit, side is known as 'debiting the account' or making a 'debit entry'. This action reflects receiving a value or benefit in that account.

Oct/Nov 2006

32. What is the fundamental rule for debit and credit concerning Personal Accounts?
(A) Debit what comes in, Credit what goes out
(B) Debit the receiver, Credit the giver
(C) Debit all expenses and losses, Credit all incomes and gains
(D) Debit the giver, Credit the receiver

Ans :

(B) Debit the receiver, Credit the giver
The golden rule for Personal Accounts focuses on the person or entity involved in the transaction. The account of the person who receives a benefit (such as cash, goods, or services) from the business is debited. The account of the person who gives a benefit to the business is credited. This rule applies to all personal account types.

May/June 2021

33. When a business purchases furniture for cash, which accounts are affected and how?
(A) Furniture account is credited, and Cash account is debited.
(B) Purchases account is debited, and Cash account is credited.
(C) Furniture account is debited, and Cash account is credited.
(D) Furniture account is debited, and Sales account is credited.

Ans :

(C) Furniture account is debited, and Cash account is credited.
Both Furniture and Cash are Real Accounts. The rule for Real Accounts is "Debit what comes in, Credit what goes out." In this transaction, furniture is coming into the business, so the Furniture account is debited. Cash is going out of the business, so the Cash account is credited. This accurately reflects the exchange of assets.

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Oct/Nov 2010

34. What is the accounting rule for Nominal Accounts?
(A) Debit the receiver, Credit the giver
(B) Debit what comes in, Credit what goes out
(C) Debit all assets, Credit all liabilities
(D) Debit all expenses and losses, Credit all incomes and gains

Ans :

(D) Debit all expenses and losses, Credit all incomes and gains
Nominal accounts track the financial performance of a business. The rule dictates that all business expenses (like salaries, rent paid) and losses (like loss by fire) are debited. Conversely, all business incomes (like sales, interest received) and gains (like profit on sale of an asset) are credited to their respective nominal accounts.

May/June 2005

35. A business pays salary to a clerk. Which two accounts are involved and what is the correct journal entry?
(A) Debit Salary Account, Credit Cash Account
(B) Debit Cash Account, Credit Salary Account
(C) Debit Clerk's Account, Credit Cash Account
(D) Debit Drawings Account, Credit Salary Account

Ans :

(A) Debit Salary Account, Credit Cash Account
The two accounts affected are Salary Account and Cash Account. Salary is an expense, and as per the rule for nominal accounts, expenses are debited. So, Salary Account is debited. Cash is an asset that is going out of the business, and as per the rule for real accounts, what goes out is credited. Hence, Cash Account is credited.

Oct/Nov 2022

36. Based on the summary table of debit and credit rules:

Types of Account	Debit	Credit
Personal	The Receiver	The Giver
Real	What Comes in	What Goes out
Nominal	Expenses or Losses	Incomes or Gains

If a business receives interest, what is the correct application of these rules?
(A) Debit Interest Account as it is an expense, and Credit Cash Account as it goes out.
(B) Debit Cash Account as it comes in, and Credit Interest Account as it is an income.
(C) Debit Cash Account as it is the receiver, and Credit Interest Account as it is the giver.
(D) Debit Interest Account as it comes in, and Credit Cash Account as it goes out.

Ans :

(B) Debit Cash Account as it comes in, and Credit Interest Account as it is an income.
When interest is received, cash (a Real Account) comes into the business, so the Cash Account is debited based on the "What Comes in" rule. The interest received is an income for the business. Interest is a Nominal Account, and according to the rule, all incomes and gains are credited. Therefore, the Interest Account is credited.

May/June 2018

37. If a firm borrows ₹10,000 and at the end of the year, interest of ₹1,200 is due but not yet paid, what entry is made to record this obligation?
(A) Debit Cash Account, Credit Interest Account
(B) Debit Interest Account, Credit Cash Account
(C) Debit Lender's Account, Credit Interest Account
(D) Debit Interest Account, Credit Lender's Account

Ans :

(D) Debit Interest Account, Credit Lender's Account
Even if cash is not paid, the expense has been incurred and an obligation has arisen. Interest is an expense (Nominal Account), so the Interest Account is debited. Since the amount is not paid, it increases the amount owed to the lender. The lender is the giver of the extended credit, so the Lender's Account (Personal Account) is credited.

NODIA

Oct/Nov 2016

38. What does a new debit entry in a Personal Account imply if the account did not exist before?
(A) The person has become a debtor of the business.
(B) The person has become a creditor of the business.
(C) The business has incurred an expense related to that person.
(D) The business has earned income from that person.

Ans :

(A) The person has become a debtor of the business.
A debit to a personal account follows the rule "Debit the receiver." When a new personal account is opened with a debit, it signifies that the person has received a benefit (like goods on credit) from the business for the first time and now owes money to the business. This establishes them as a debtor.

May/June 2014

39. If a person who is a creditor of the business has their account debited, what does this imply?
(A) The amount due to that person has increased.
(B) The amount due from that person has increased.
(C) The amount due to that person has decreased.
(D) The business has made an additional purchase from them on credit.

Ans :

(C) The amount due to that person has decreased.
A creditor has a credit balance, representing the amount the business owes them. When this creditor's account is debited (e.g., when a payment is made to them), it signifies they are the receiver of the payment. This debit entry reduces the liability of the business towards them, thus decreasing the amount due to that person.

Oct/Nov 2007

40. What is the significance of a credit entry in a Real Account?
(A) The business has disposed of a part or the whole of the asset.
(B) The value of the asset has increased.
(C) The business has acquired more of that asset.
(D) The asset has become an expense for the business.

Ans :

(A) The business has disposed of a part or the whole of the asset.
The rule for Real Accounts is "Credit what goes out." A credit entry in a real account, such as Plant & Machinery or Cash, signifies that the asset is leaving the business or its value is decreasing. This happens, for example, when an asset is sold or when cash is paid out for an expense.

May/June 2025

41. A debit in a Nominal Account signifies that:
(A) There has been an income or profit.
(B) An asset has been acquired.
(C) A liability has been created.
(D) An expense or loss has been incurred.

Ans :

(D) An expense or loss has been incurred.
The rule for Nominal Accounts is "Debit all expenses and losses." Therefore, a debit entry in a nominal account like Salaries, Rent, or Loss by Fire indicates that the business has incurred an expense or suffered a loss. This entry serves to record the reduction in the business's profit or equity for the period.

Oct/Nov 2019

42. Pranab gives a loan of ₹500 to Nanda. In the books of Pranab, what is the correct accounting treatment?
(A) Pranab's Account is debited, and Cash Account is credited.
(B) Nanda's Account is debited, and Cash Account is credited.
(C) Cash Account is debited, and Nanda's Account is credited.
(D) Loan Account is credited, and Nanda's Account is debited.

Ans :

(B) Nanda's Account is debited, and Cash Account is credited.
In this transaction, Nanda is the receiver of the cash (benefit). As per the rule for personal accounts, the receiver is debited. So, Nanda's Account is debited. Cash is an asset (real account) that is going out of Pranab's business. As per the rule for real accounts, what goes out is credited. Therefore, Cash Account is credited.

Oct/Nov 2015

43. Sushma withdraws ₹10,000 from Dena Bank. In the books of Sushma, what is the correct entry?
(A) Sushma's Account Dr. To Dena Bank Account
(B) Dena Bank Account Dr. To Cash Account
(C) Cash Account Dr. To Dena Bank Account
(D) Drawings Account Dr. To Dena Bank Account

Ans :

(C) Cash Account Dr. To Dena Bank Account
When Sushma withdraws cash from the bank, cash (a real account) comes into the business's cash box. Therefore, the Cash Account is debited. Dena Bank (an artificial personal account) is the

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giver of the money. According to the personal account rule, the giver is credited. Hence, Dena Bank Account is credited.

May/June 2012

44. Prasad purchased goods worth ₹5,000 from Ram on credit. In Prasad's books, which accounts are debited and credited?
(A) Ram's Account Dr. To Purchases Account
(B) Goods Account Dr. To Ram's Account
(C) Goods Account Dr. To Cash Account
(D) Purchases Account Dr. To Ram's Account

Ans :

(D) Purchases Account Dr. To Ram's Account
In this transaction, goods are coming into the business. The purchase of goods is recorded by debiting the Purchases Account (a nominal account representing an expense). Ram is the giver of the goods on credit. As per the personal account rule, the giver is credited. Therefore, Ram's Account is credited in Prasad's books.

Oct/Nov 2022

45. A trader pays ₹1,500 to his manager as salary. In the trader's books, what is the correct journal entry?
(A) Salary Account Dr. To Cash Account
(B) Manager's Account Dr. To Cash Account
(C) Cash Account Dr. To Salary Account
(D) Drawings Account Dr. To Cash Account

Ans :

(A) Salary Account Dr. To Cash Account
Salary is a business expense, and according to the nominal account rule, all expenses are debited. Thus, Salary Account is debited. Cash, a real account, is going out of the business to make the payment. According to the real account rule, what goes out is credited. Therefore, the Cash Account is credited.

May/June 2005

46. Which of the following is NOT a feature of a cash book?
(A) Only cash transactions are recorded.
(B) It records both cash and credit transactions chronologically.
(C) It performs the functions of both the journal and the ledger.
(D) All cash receipts are recorded on the debit side.

Ans :

(B) It records both cash and credit transactions chronologically.
A defining feature of the cash book is that it is exclusively used for recording cash and bank transactions. Credit transactions, such as credit sales or credit purchases, are not recorded in the cash book. They are recorded in other specialized subsidiary books like the Sales Journal or Purchases Journal.

Oct/Nov 2008

47. A simple (single column) cash book is similar to which type of account?
(A) A personal account
(B) An ordinary cash account
(C) A nominal account
(D) A suspense account

Ans :

(B) An ordinary cash account
A simple cash book is essentially a cash account presented in a columnar book format. It has two sides, debit and credit, just like a ledger account. All cash receipts are debited, and all cash payments are credited, serving the exact function of a standard cash ledger account, which is why a separate cash account is not needed.

NODIA

May/June 2006

48. In the proforma of a single column cash book, what does 'Vr. No.' on the credit side stand for?
(A) Voucher Number
(B) Verification Number
(C) Volume Reference
(D) Value Received

Ans :

(A) Voucher Number
On the payments (credit) side of a cash book, the 'Vr. No.' column is for the Voucher Number. For every payment made by a business, a supporting document called a voucher is prepared as evidence. These vouchers are serially numbered, and this number is recorded in the 'Vr. No.' column for reference and audit trail purposes.

Oct/Nov 2017

49. What are the main source documents for recording entries on the receipts (debit) side of the cash book?
(A) Vouchers and cheque book counterfoils
(B) Invoices from suppliers
(C) Official receipts and cash memos

(D) Debit notes issued to customers

Ans :

(C) Official receipts and cash memos
The debit side of the cash book records all cash inflows. The primary evidence for these receipts comes from cash memos issued for cash sales and the carbon copies of official receipts issued to customers when they make payments. These documents provide the necessary details like date, amount, and payer for making the entry.

May/June 2008

50. When posting an entry from the debit (receipts) side of the cash book to a ledger account, what entry is made in the concerned ledger account?
(A) The account is credited by writing 'By Cash a/c'.
(B) The account is debited by writing 'To Cash a/c'.
(C) The account is debited by writing 'By Cash a/c'.
(D) The account is credited by writing 'To Cash a/c'.

Ans :

(A) The account is credited by writing 'By Cash a/c'.
The cash book itself acts as the debit aspect (Cash Dr.) for a receipt transaction. To complete the double entry, the corresponding credit must be posted to the ledger. For example, if cash is received from Ramesh, the entry in the cash book is 'To Ramesh'. The posting in Ramesh's ledger account will be on the credit side as 'By Cash a/c'.

Oct/Nov 2013

51. In balancing a cash book, why will the debit side total always be more than or equal to the credit side total?
(A) Because receipts are always higher than payments.
(B) The cash book must always show a profit.
(C) Because a business cannot pay more cash than it has.
(D) Because of the 'debit the receiver' rule.

Ans :

(C) Because a business cannot pay more cash than it has.
The cash book records the flow of physical cash. A business's cash payments (credits) can never exceed its cash receipts and opening balance (debits), as it is impossible to spend more cash than is available. Therefore, the cash book can only have a debit balance (more receipts than payments) or a zero balance, but never a credit balance.

May/June 2015

52. What do the two columns on each side of a double columnar cash book represent?
(A) Cash and Bank
(B) Cash and Sales
(C) Discount and Purchases
(D) Cash and Discount

Ans :

(D) Cash and Discount
A double columnar cash book expands on the simple cash book by adding a 'Discount' column next to the 'Cash' column on both the debit and credit sides. The discount column on the debit side records 'Discount Allowed' on receipts, while the one on the credit side records 'Discount Received' on payments.

Oct/Nov 2012

53. In a double column cash book, the discount columns are described as 'memorandum columns'. What does this mean?
(A) They are the most important columns in the cash book.
(B) They do not serve the function of a discount account and are just for noting purposes.
(C) Their balances are carried forward to the next period.
(D) They are totaled and balanced just like the cash columns.

Ans :

(B) They do not serve the function of a discount account and are just for noting purposes.
The discount columns are for informational or memorandum purposes only. Unlike the cash columns, they are not balanced. Instead, the totals of the 'Discount Allowed' (debit side) and 'Discount Received' (credit side) columns are posted as lump sums to the respective 'Discount Allowed Account' and 'Discount Received Account' in the general ledger.

May/June 2011

54. **Assertion (A) :** The totals of the discount columns in a double column cash book are posted to the respective discount accounts in the ledger.

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Reason (R) : The discount columns in a double column cash book function as the actual Discount Allowed and Discount Received accounts.

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(C) (A) is true but (R) is false.
Assertion (A) is true; the totals of the debit and credit discount columns are posted to the Discount Allowed and Discount Received ledger accounts, respectively. However, Reason (R) is false. The discount columns themselves are merely memorandum columns for recording discounts; they do not function as the actual ledger accounts.

Oct/Nov 2020

55. On Dec 2, a firm sold goods to Sharad for ₹3,000 and received half the amount in cash after allowing a 5% cash discount. What entry will be made in the double column cash book?
(A) Debit Cash ₹1,500; Debit Discount ₹75.
(B) Debit Cash ₹1,500; No discount entry.
(C) Debit Cash ₹3,000; Debit Discount ₹150.
(D) Debit Cash ₹1,425; Debit Discount ₹75.

Ans :

(D) Debit Cash ₹1,425; Debit Discount ₹75.
Half the amount is ₹1,500. A 5% cash discount on this amount is ₹75 (5% × ₹1,500). The cash actually received is ₹1,500 - ₹75 = ₹1,425. In the double column cash book, the cash column will be debited with ₹1,425 (cash inflow), and the discount allowed column will be debited with ₹75.

May/June 2022

56. On Dec 29, Madan's account of ₹3,000 was settled after adjusting a discount of 10%. How is this recorded on the credit side of the cash book?
(A) Cash paid ₹3,000; Discount received ₹300.
(B) Cash paid ₹2,700; Discount received ₹300.
(C) Cash paid ₹3,000; No discount entry.
(D) Cash paid ₹2,700; Discount received not recorded in cash book.

Ans :

(B) Cash paid ₹2,700; Discount received ₹300.
The total amount due to Madan is ₹3,000. A 10% discount means a discount of ₹300 (10% × ₹3,000) is received. The actual cash paid to settle the account is ₹3,000 - ₹300 = ₹2,700. On the credit (payment) side of the cash book, the Cash column will show ₹2,700 and the Discount Received column will show ₹300.

NODIA

Oct/Nov 2023

57. What are the three columns on each side of a three columnar cash book?
(A) Discount, Cash, and Sales
(B) Cash, Bank, and Purchases
(C) Date, Particulars, and Amount
(D) Discount, Cash, and Bank

Ans :

(D) Discount, Cash, and Bank
A three columnar cash book is an extension of the double column cash book. It includes three amount columns on both the debit and credit sides: one for discount, one for cash transactions, and one for bank transactions. This allows for the simultaneous recording of cash and bank receipts and payments in one place.

May/June 2016

58. In a three columnar cash book, which accounting rule is applied for transactions in the bank column?
(A) The rule for Personal Accounts (Debit the receiver, Credit the giver).
(B) The rule for Real Accounts (Debit what comes in, Credit what goes out).
(C) The rule for Nominal Accounts (Debit expenses, Credit incomes).
(D) The rule for assets (Debit increases, Credit decreases).

Ans :

(A) The rule for Personal Accounts (Debit the receiver, Credit the giver).
The bank account maintained by the enterprise represents the account of the banking company, which is an artificial person. Therefore, transactions recorded in the bank column must follow the rule for personal accounts. The bank is debited when it is the receiver (e.g., cash deposited), and it is credited when it is the giver (e.g., cash withdrawn).

Oct/Nov 2009

59. What is a 'Contra Entry' in a three columnar cash book?

(A) An entry that is recorded only on the debit side.
(B) An entry to record the purchase or sale of goods on credit.
(C) A transaction involving both cash and bank accounts, recorded on both sides of the cash book.
(D) An entry that corrects a previous error in the cash book.

Ans :

(C) A transaction involving both cash and bank accounts, recorded on both sides of the cash book.
A contra entry records a transaction that affects both the cash and bank balances, such as depositing cash into the bank or withdrawing cash from the bank for office use. It is recorded on both the debit and credit sides of the three-column cash book to complete the double entry within the cash book itself, and is denoted by 'C' in the L.F. column.

May/June 2023

60. When cash is withdrawn from the bank for office use, how is the contra entry recorded in the three columnar cash book?

(A) Debited in the bank column and credited in the cash column.
(B) Debited in the cash column and credited in the bank column.
(C) Debited in the cash column and credited in the discount column.
(D) Credited in the cash column and debited in the discount column.

Ans :

(B) Debited in the cash column and credited in the bank column.
When cash is withdrawn from the bank, the cash balance in the office increases, so the cash column is debited ("what comes in"). The bank is the giver of the money, so the bank column is credited ("credit the giver"). This transaction is recorded on both sides of the cash book and marked as a contra entry.

Oct/Nov 2018

61. Consider the following transaction from Illustration 6: "Dec 10: Cash deposited into Bank ₹5,000." How is this contra entry correctly recorded in the three-column cash book?

(A) A debit of ₹5,000 in the Cash column and a credit of ₹5,000 in the Bank column.
(B) A debit of ₹5,000 in the Bank column only.
(C) A credit of ₹5,000 in the Cash column only.
(D) A debit of ₹5,000 in the Bank column and a credit of ₹5,000 in the Cash column.

Ans :

(D) A debit of ₹5,000 in the Bank column and a credit of ₹5,000 in the Cash column.
When cash is deposited into the bank, the bank is the receiver, so the Bank column on the debit side is increased by ₹5,000. Simultaneously, cash is going out of the business's cash box, so the Cash column on the credit side is decreased by ₹5,000. This is a classic contra entry, reflected on both sides of the cash book.

May/June 2007

62. In Illustration 6, on Dec 4, a payment is made to Navjot by cheque for ₹450 in full settlement of ₹470. How would this be recorded in the three-column cash book?

(A) Credit Bank ₹470, Credit Discount ₹20.
(B) Credit Bank ₹450, Credit Discount ₹20.
(C) Credit Cash ₹450, Credit Discount ₹20.
(D) Credit Bank ₹450, Debit Discount ₹20.

Ans :

(B) Credit Bank ₹450, Credit Discount ₹20.
The payment is made by cheque, so the bank is the giver. The Bank column on the credit side is credited with the actual amount paid, which is ₹450. The difference of ₹20 (₹470 - ₹450) is a discount received by the business. This is recorded in the Discount column on the credit (payment) side.

Oct/Nov 2025

63. As per Illustration 6, on Dec 15, the bank debited ₹20 for bank charges. How is this transaction recorded in Mamta's cash book?

(A) A debit of ₹20 in the Bank column under 'By Bank Charges'.
(B) A debit of ₹20 in the Cash column under 'To Bank Charges'.
(C) A credit of ₹20 in the Bank column under 'By Bank Charges'.
(D) A credit of ₹20 in the Cash column under 'By Bank Charges'.

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Ans :

(C) A credit of ₹20 in the Bank column under 'By Bank Charges'.
Bank charges represent an expense for the business and a reduction in the bank balance. The bank is effectively taking money from the account. Following the personal account rule, the bank is the giver of this service cost, or alternatively, the bank balance is reduced. Therefore, the Bank column on the credit side is credited with ₹20.

May/June 2012

64. In Illustration 6, on Dec 18, Saba directly deposited a cheque for ₹3,500 into the bank. What is the entry in the cash book?
(A) Debit Cash column with ₹3,500.
(B) Credit Bank column with ₹3,500.
(C) Credit Cash column with ₹3,500.
(D) Debit Bank column with ₹3,500.

Ans :

(D) Debit Bank column with ₹3,500.
When a customer deposits a cheque directly into the business's bank account, the bank balance increases. The bank is the receiver of the funds on behalf of the business. Therefore, the Bank column on the debit (receipts) side of the cash book is debited with the amount of ₹3,500 to reflect this increase.

Oct/Nov 2014

65. On Dec 13 of Illustration 6, Sunil's cheque of ₹2,100 was endorsed to Vinod in full settlement of ₹2,150. What is the correct journal entry for this transaction as seen from the ledger postings?
(A) Vinod Dr. ₹2,150; To Cheques in Hand ₹2,100; To Discount Received ₹50.
(B) Vinod Dr. ₹2,150; To Sunil ₹2,100; To Discount Received ₹50.
(C) Vinod Dr. ₹2,100; Discount Allowed Dr. ₹50; To Sunil ₹2,150.
(D) Vinod Dr. ₹2,150; To Cash ₹2,100; To Discount Received ₹50.

Ans :

(A) Vinod Dr. ₹2,150; To Cheques in Hand ₹2,100; To Discount Received ₹50.
Vinod's account is settled for ₹2,150, so his account is debited by the full amount to clear the liability. The cheque on hand (from Sunil) worth ₹2,100 is given away. The remaining ₹50 is a discount received from Vinod. The entry in Vinod's ledger account reflects a debit of ₹2,150, which is settled by giving the cheque and receiving a discount.

May/June 2019

66. What is the primary purpose of maintaining a Petty Cash Book?
(A) To record all major capital expenditures of the business.
(B) To avoid burdening the main cash book with numerous small payments.
(C) To record large volume credit sales and purchases.
(D) To track payments made exclusively by cheque.

Ans :

(B) To avoid burdening the main cash book with numerous small payments.
Businesses make many small, repetitive payments daily for expenses like postage, stationery, and conveyance. Recording each of these in the main cash book would make it bulky and difficult to manage. A petty cash book is a subsidiary book specifically designed to handle these small-value (petty) expenses, thus keeping the main cash book clean.

Oct/Nov 2006

67. The person who maintains the petty cash book and makes small payments is known as the:
(A) Chief Cashier
(B) Accountant
(C) Auditor
(D) Petty Cashier

Ans :

(D) Petty Cashier
A specific person, designated as the petty cashier, is entrusted with a certain amount of cash to make small payments on behalf of the business. This individual is responsible for disbursing the money for authorized petty expenses, obtaining receipts, and maintaining the petty cash book, which is a record of all such payments.

May/June 2021

68. In a simple petty cash book, on which side is the amount received from the main cashier recorded?
(A) On the debit side.
(B) On the credit side.
(C) On both the debit and credit sides.

NODIA

(D) It is not recorded in the petty cash book.

Ans :

(A) On the debit side.
A simple petty cash book operates like a mini-cash account. The amount of cash received by the petty cashier from the chief cashier is a receipt for the petty cash fund. All receipts are recorded on the debit side, representing an increase in the cash available for petty expenses. All payments are then recorded on the credit side.

Oct/Nov 2010

69. What is the main advantage of a Columnar or Analytical Petty Cash Book over a Simple Petty Cash Book?
(A) It has fewer columns and is easier to prepare.
(B) It can be used to record credit transactions.
(C) It allows for the analysis of petty expenses under various heads.
(D) Each payment does not require a supporting voucher.

Ans :

(C) It allows for the analysis of petty expenses under various heads.
The columnar petty cash book has separate analysis columns for frequent expense categories (e.g., Postage, Conveyance, Stationery). This format allows for the periodic total of each expense type to be posted as a single amount to the ledger, saving time and providing a convenient analysis of where petty cash is being spent.

May/June 2005

70. The amount given by the chief cashier to the petty cashier from time to time to make small payments is called:
(A) Petty cash
(B) Petty loan
(C) Petty capital
(D) Petty drawing

Ans :

(A) Petty cash
The sum of money advanced by the chief cashier to the petty cashier to cover minor expenses for a specific period is known as petty cash. The petty cashier makes payments from this fund and records them. The system ensures that a controlled amount of cash is available for small, necessary expenditures without complex approval processes.

Oct/Nov 2022

71. What is the 'Imprest System' of petty cash?
(A) A system where the petty cashier can draw any amount of cash as needed.
(B) A system where all petty expenses are paid directly by the chief cashier.
(C) A system used only for recording petty incomes, not expenses.
(D) A system where a fixed sum is given, and at the end of the period, the exact amount spent is reimbursed.

Ans :

(D) A system where a fixed sum is given, and at the end of the period, the exact amount spent is reimbursed.
Under the imprest system, the petty cashier starts with a fixed float (the imprest amount). At the end of a period, they submit expense records. The chief cashier then reimburses the exact amount spent, bringing the petty cash balance back up to the original imprest amount. This provides excellent control over petty expenses.

May/June 2018

72. Since there is no unnecessary accumulation of cash in hand, chances of defalcation of cash are minimised. This advantage of the Imprest System is achieved primarily because:
(A) The chief cashier personally verifies every single transaction before payment.
(B) The petty cashier has to estimate requirements for a period and is not allowed to draw cash whenever desired.
(C) All payments are made through bank transfers instead of cash.
(D) The imprest amount is increased every week automatically.

Ans :

(B) The petty cashier has to estimate requirements for a period and is not allowed to draw cash whenever desired.
The imprest system controls cash by limiting the petty cashier's ability to draw funds arbitrarily. They receive a fixed amount based on an estimate for a period. This prevents the buildup of a large, unnecessary cash balance in the hands of the petty cashier, thereby reducing the temptation and opportunity for misappropriation or defalcation.

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Oct/Nov 2016

73. On Jan 1, a petty cashier is given an imprest amount of ₹200. During the week, they spend ₹198 on various expenses. Under the imprest system, how much cash will the chief cashier give to the petty cashier at the start of the next week?
(A) ₹200
(B) ₹2
(C) ₹198
(D) ₹398

Ans :

(C) ₹198
The core principle of the imprest system is to restore the petty cashier's float to the original amount. The petty cashier started with ₹200 and spent ₹198, leaving a balance of ₹2. To bring the cash in hand back to the imprest amount of ₹200, the chief cashier will reimburse the exact amount that was spent, which is ₹198.

May/June 2014

74. In Illustration 8, the imprest amount is ₹250. The total expenses for March amount to ₹217. What is the closing balance c/d on the last day of March, and what amount is received on April 1 to restore the imprest?
(A) Closing balance ₹250; Amount received ₹217.
(B) Closing balance ₹217; Amount received ₹33.
(C) Closing balance ₹33; Amount received ₹250.
(D) Closing balance ₹33; Amount received ₹217.

Ans :

(D) Closing balance ₹33; Amount received ₹217.
The initial imprest amount was ₹250. The total expenses incurred during the period were ₹217. The remaining cash, or the closing balance carried down (c/d), is the initial amount minus the expenses: ₹250 - ₹217 = ₹33. To restore the imprest to ₹250 for the next period, the chief cashier will reimburse the exact amount spent, which is ₹217.

Oct/Nov 2007

75. The process of recording transactions in a journal is termed as:
(A) Journalising
(B) Posting
(C) Balancing
(D) Auditing

Ans :

(A) Journalising
'Journalising' is the specific accounting term for the process of analyzing a business transaction to identify the debit and credit aspects and then recording it in the journal in a chronological order. This process creates the first formal accounting record of a transaction and includes the date, accounts involved, amounts, and a narration.

May/June 2025

76. Specialized journals like the 'Purchase Book' are used to record what specific type of transaction?
(A) All purchases, including cash and credit.
(B) Only credit purchases of goods-in-trade.
(C) Only cash purchases of assets.
(D) All returns of goods to suppliers.

Ans :

(B) Only credit purchases of goods-in-trade.
To streamline the recording process, specialized journals are used for high-volume, repetitive transactions. The Purchase Book (or Purchases Journal) is exclusively used to record the purchase of goods-in-trade on a credit basis. Cash purchases are recorded in the cash book, and credit purchases of assets are recorded in the general journal.

Oct/Nov 2019

77. Which of the following is NOT one of the five standard columns in a general journal?
(A) Date
(B) Particulars
(C) Ledger Folio (L.F.)
(D) Voucher Number

Ans :

(D) Voucher Number
The standard ruling of a general journal consists of five columns: (i) Date, to record when the transaction occurred; (ii) Particulars, to record the accounts being debited and credited and the narration; (iii) Ledger Folio (L.F.), for cross-referencing; (iv) Amount (Debit); and (v) Amount (Credit). A voucher number column is not standard in a general journal.

May/June 2009

78. In the 'Particulars' column of a journal, how is the account to be credited typically written?
(A) On the next line, slightly indented, and prefixed with 'To'.
(B) On the same line as the debit account,

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prefixed with 'By'.
(C) On the next line, starting from the extreme left, prefixed with 'Cr.'.
(D) Below the narration, prefixed with 'Credit:'.

Ans :

(A) On the next line, slightly indented, and prefixed with 'To'.
By convention, when journalising, the account to be debited is written first, aligned to the left margin. The account to be credited is written on the subsequent line. This credit account title is indented to the right and is traditionally prefixed with the word 'To' to clearly distinguish it from the debit entry.

Oct/Nov 2011

79. What is a 'narration' in a journal entry?
(A) The page number of the ledger where the entry is posted.
(B) The total of the debit and credit columns.
(C) A brief explanation of the transaction written below the debit and credit entries.
(D) The name of the person who authorized the transaction.

Ans :

(C) A brief explanation of the transaction written below the debit and credit entries.
A narration is a concise description of the business transaction that is being recorded. It is written in the 'Particulars' column, usually in brackets, immediately after the credit account entry. Its purpose is to provide context and clarity, making it easier to understand the reason for the journal entry at a later date.

May/June 2010

80. A journal entry that involves more than one debit and/or more than one credit is known as a:
(A) Compound Journal Entry
(B) Contra Entry
(C) Opening Entry
(D) Reversing Entry

Ans :

(A) Compound Journal Entry
A compound journal entry is a single entry that affects three or more accounts. This is used to record interconnected transactions that occur simultaneously, such as paying for multiple expenses with a single cheque. The key rule for a compound entry is that the sum of all debit amounts must equal the sum of all credit amounts.

Oct/Nov 2024

81. When journal entries extend over several pages, what do the notations 'Total c/f' and 'Total b/f' signify?
(A) 'c/f' means credit forward, and 'b/f' means balance forward.
(B) 'c/f' means cash forward, and 'b/f' means bank forward.
(C) 'c/f' means closing figure, and 'b/f' means beginning figure.
(D) 'c/f' means carried forward, and 'b/f' means brought forward.

Ans :

(D) 'c/f' means carried forward, and 'b/f' means brought forward.
To ensure the equality of debits and credits across pages, the debit and credit columns are totaled at the bottom of each journal page. This total is marked 'Total c/f' (carried forward). On the top of the very next page, the same totals are written and marked 'Total b/f' (brought forward) before new entries are recorded.

May/June 2017

82. If a transaction states "Sold goods ₹2,000" without mentioning the name of the party or whether it was for cash, how should it be treated?
(A) As a credit transaction, debiting Debtors Account.
(B) As a cash transaction, debiting Cash Account.
(C) It should not be recorded until more information is available.
(D) As a partial cash and partial credit transaction.

Ans :

(B) As a cash transaction, debiting Cash Account.
A standard accounting convention dictates that if a transaction does not specify whether it is for cash or on credit and the name of the other party is not given, it should be assumed to be a cash transaction. Therefore, "Sold goods ₹2,000" implies cash was received, and the entry would be to debit Cash and credit Sales.

Oct/Nov 2005

83. When the words 'Received' or 'Paid' appear in a transaction description, what does it always imply?
(A) The transaction is on a credit basis.

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(B) The transaction involves the movement of goods.
(C) The transaction involves cash being received or paid.
(D) The transaction requires a compound journal entry.

Ans :

(C) The transaction involves cash being received or paid.
The terms 'Received' and 'Paid' are explicit indicators of a cash or bank transaction. 'Paid salaries' means cash has been paid out, and 'Received interest' means cash has come in. These words remove any ambiguity about whether the transaction was on a cash or credit basis, confirming the involvement of the cash or bank account.

May/June 2020

84. When goods are returned by a customer, which account should be used to record the transaction?
(A) Purchases Return Account
(B) Sales Account
(C) Customer's Personal Account only
(D) Sales Return or Returns Inward Account

Ans :

(D) Sales Return or Returns Inward Account
When a customer returns goods previously sold to them, it is recorded in the 'Sales Return Account' or 'Returns Inward Account'. This account is specifically used to track the value of goods coming back into the business from customers. It is typically debited, as it represents a reversal of sales revenue.

Oct/Nov 2015

85. What is the purpose of an 'Opening Entry'?
(A) To carry forward the balances of real and personal accounts from the previous year to the current year.
(B) To record the very first transaction of a new business.
(C) To close all nominal accounts at the end of the year.
(D) To record the receipt of cash from the issue of shares.

Ans :

(A) To carry forward the balances of real and personal accounts from the previous year to the current year.
At the end of an accounting year, asset, liability, and capital accounts (Real and Personal accounts) have closing balances that appear on the Balance Sheet. An opening entry is the first journal entry passed in the new accounting year to bring these closing balances forward as the opening balances for the current year's books.

May/June 2013

86. Mr. Prasad has the following balances on Dec 31, 2022: Cash ₹2,500; Stock ₹22,500; Furniture ₹10,000; Debtors ₹12,000; Bank Loan ₹8,000; Capital ₹39,000. Which of the following represents the correct opening journal entry on Jan 1, 2023?
(A) Credit all assets, Debit all liabilities and capital.
(B) Debit all assets, Credit all liabilities and capital.
(C) Debit Cash, Stock, Furniture; Credit Debtors, Bank Loan, Capital.
(D) Debit Bank Loan, Capital; Credit Cash, Stock, Furniture, Debtors.

Ans :

(B) Debit all assets, Credit all liabilities and capital.
In an opening entry, all asset accounts are debited to bring forward their opening balances, as assets normally have debit balances. All liability and capital accounts are credited to bring forward their opening balances, as they normally have credit balances. This entry establishes the starting financial position for the new accounting period in the journal.

Oct/Nov 2021

87. In Illustration 10, Kesari commenced business with ₹15,000, of which ₹5,000 was a loan from his wife at 12% interest. What is the correct journal entry for this transaction?
(A) Cash a/c Dr. 15,000; To Capital a/c 15,000.
(B) Cash a/c Dr. 10,000; Loan from Mrs Kesari a/c Dr. 5,000; To Capital a/c 15,000.
(C) Capital a/c Dr. 10,000; Loan from Mrs Kesari a/c Dr. 5,000; To Cash a/c 15,000.
(D) Cash a/c Dr. 15,000; To Capital a/c 10,000; To Loan from Mrs Kesari a/c 5,000.

Ans :

(D) Cash a/c Dr. 15,000; To Capital a/c 10,000; To Loan from Mrs Kesari a/c 5,000.

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The total cash coming into the business is ₹15,000, so Cash Account is debited. This cash comes from two sources: ₹10,000 from the owner (Capital) and ₹5,000 from his wife (a liability). Therefore, Capital Account is credited with ₹10,000 and the liability account, 'Loan from Mrs Kesari', is credited with ₹5,000.

May/June 2024

88. On Feb 6, Kesari bought goods from Satish for ₹6,000. Half of these goods were sold to Nayan at 30% above cost. What is the amount debited to Nayan's account?
(A) ₹3,900
(B) ₹3,000
(C) ₹6,000
(D) ₹1,800

Ans :

(A) ₹3,900
The cost of goods sold to Nayan is half of ₹6,000, which is ₹3,000. The goods were sold at a 30% profit on cost. The profit is 30% × ₹3,000 = ₹900. The selling price is the cost plus profit, which is ₹3,000 + ₹900 = ₹3,900. Since this is a credit sale, Nayan (the receiver/debtor) is debited with the full invoice amount of ₹3,900.

Oct/Nov 2008

89. On Feb 22, Ambar, who owed ₹1,200, became insolvent, and a dividend of 50 paise in a rupee was received. What is the amount of Bad Debts to be recorded?
(A) ₹1,200
(B) ₹50
(C) ₹600
(D) ₹2,400

Ans :

(C) ₹600
The total amount due from Ambar was ₹1,200. A dividend of 50 paise in a rupee means 50% of the due amount is recovered. The amount received is 50% × ₹1,200 = ₹600. The remaining amount that could not be recovered is the loss to the business, known as a bad debt. This is ₹1,200 - ₹600 = ₹600.

May/June 2006

90. On Feb 28, Kesari paid ₹350 for monthly charges to the Housing Society for his own residence. How should this transaction be recorded?
(A) Drawings a/c Dr. To Cash a/c
(B) Office Expenses a/c Dr. To Cash a/c
(C) Housing Society a/c Dr. To Cash a/c
(D) Miscellaneous Expenses a/c Dr. To Cash a/c

Ans :

(A) Drawings a/c Dr. To Cash a/c
The payment is for the owner's personal residence, not for a business expense. When business funds are used for the personal expenses of the owner, it is treated as 'Drawings'. Therefore, the Drawings Account is debited to record the owner's withdrawal of funds, and the Cash Account is credited as cash is going out of the business.

Oct/Nov 2017

91. Which of the following statements is incorrect regarding the rules of debit and credit?
(A) For a Personal Account, the receiver is debited and the giver is credited.
(B) For a Real Account, what comes in is debited and what goes out is credited.
(C) For a Nominal Account, all incomes and gains are debited.
(D) The debit effect is always recorded first in a journal entry before the credit effect.

Ans :

(C) For a Nominal Account, all incomes and gains are debited.
The statement that all incomes and gains are debited for a Nominal Account is incorrect. The golden rule for nominal accounts is "Debit all expenses and losses, and Credit all incomes and gains." Therefore, incomes and gains are credited, not debited. The other statements correctly describe established accounting conventions and rules.

May/June 2008

92. Identify the incorrect statement regarding the cash book.
(A) It keeps records of all cash receipts and cash payments.
(B) All receipts are recorded on the credit side.
(C) It is divided into two sides, viz., debit and credit.
(D) It functions as both a journal and a ledger.

Ans :

(B) All receipts are recorded on the credit side.
This statement is incorrect. The cash book functions as a cash account, which is a real account. The rule for real accounts is "Debit

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what comes in, Credit what goes out." Therefore, all cash receipts (cash coming in) are recorded on the debit side, and all cash payments (cash going out) are recorded on the credit side.

Oct/Nov 2013

93. Which of the following statements about the journal and ledger is incorrect?
(A) The ledger is the book of first entry.
(B) The journal is a book for chronological record, while the ledger is for analytical record.
(C) Journal is considered more reliable compared to the ledger.
(D) 'Posting' is the term for transferring entries from the journal to the ledger.

Ans :

(A) The ledger is the book of first entry.
This statement is incorrect. The journal is the book of first or original entry, where transactions are initially recorded. The ledger is the book of second entry, where entries from the journal are classified and posted into respective accounts. The process flows from journal to ledger, not the other way around.

May/June 2015

94. A limited company's account, such as 'ABC Ltd. a/c', is an example of which type of account?
(A) Nominal account
(B) Natural Personal account
(C) Artificial Personal account
(D) Representative Personal account

Ans :

(C) Artificial Personal account
An artificial personal account pertains to corporate bodies or institutions that are treated as separate legal entities in business dealings. A limited company is created by law and functions as a legal person. Therefore, its account is classified as an artificial personal account, distinct from accounts of individuals (natural) or groups (representative).

Oct/Nov 2012

95. Goodwill and trademarks are examples of which type of account?
(A) Intangible Nominal account
(B) Nominal account
(C) Personal account
(D) Real account

Ans :

(D) Real account
Goodwill and trademarks are assets of the business. Accounts related to assets and properties are classified as Real Accounts. Specifically, since they lack physical substance but have monetary value, they are categorized as Intangible Real Accounts. They are not nominal accounts because they are not expenses or incomes, but valuable properties owned by the business.

May/June 2011

96. Match List-I with List-II and select the correct answer using the codes given below.

	List I (Account Type)		**List II (Example)**
P.	Natural Personal	1.	Bank Account
Q.	Artificial Personal	2.	Santosh's Account
R.	Representative Personal	3.	Land and Building
S.	Tangible Real	4.	Salary Outstanding

Code:
(A) P-2, Q-1, R-4, S-3
(B) P-1, Q-2, R-3, S-4
(C) P-2, Q-4, R-1, S-3
(D) P-4, Q-1, R-2, S-3

Ans :

(A) P-2, Q-1, R-4, S-3
Santosh's Account is a Natural Personal account (P-2). A Bank Account represents the banking company, an Artificial Personal account (Q-1). Salary Outstanding represents employees to whom salary is due, making it a Representative Personal account (R-4). Land and Building is a physical asset, hence a Tangible Real account (S-3).

Oct/Nov 2020

97. Consider the following statements about posting from journal to ledger:
1. The concerned account debited in the journal should be debited in the ledger.
2. It is customary to use the words 'To' on the debit side and 'By' on the credit side.
3. The page number of the journal is written in the L.F. column of the ledger.

Which of the above statements are correct?
(A) 1 and 2 only
(B) 2 and 3 only

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(C) 1 and 3 only
(D) 1, 2 and 3

Ans :

(A) 1 and 2 only
Statements 1 and 2 are correct rules for posting. The debit in the journal is posted to the debit side of the ledger account, and the use of 'To' and 'By' is a standard convention. Statement 3 is incorrect; the page number of the journal is written in the 'J.F.' (Journal Folio) column of the ledger, not the 'L.F.' column.

May/June 2022

98. Which of the following statements is/are correct?
Statement I : A debit balance in a real account represents a property or an asset.
Statement II : A credit balance in a personal account represents a creditor.
(A) Only I is correct.
(B) Only II is correct.
(C) Both I and II are correct.
(D) Neither I nor II is correct.

Ans :

(C) Both I and II are correct.
Both statements are correct. Real accounts relate to assets, and a debit balance signifies the existence of that asset. Personal accounts relate to persons or entities. A credit balance in a personal account signifies that the business owes money to that person or entity, making them a creditor of the business.

Oct/Nov 2023

99. Identify the incorrect pair of account classification.
(A) Plant and machinery - Real account
(B) Commission received - Nominal account
(C) Bank loan - Real account
(D) Capital - Personal account

Ans :

(C) Bank loan - Real account
A Bank Loan account represents a liability to the bank, which is an artificial person. Therefore, a Bank Loan account is an Artificial Personal Account, not a Real Account. Plant and machinery is a tangible asset (Real), Commission received is an income (Nominal), and Capital represents the owner's equity (Personal).

May/June 2016

100. **Assertion (A) :** A cash book is considered a book of original entry.
Reason (R) : All cash transactions are first recorded in the cash book before being posted to other ledger accounts.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
A book of original entry is where transactions are first recorded. Since all cash and bank transactions are initially entered into the cash book chronologically, it functions as a primary record or a subsidiary journal. This initial recording is the reason it is classified as a book of original entry. Therefore, both statements are true and R correctly explains A.

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Oct/Nov 2009

101. Consider the following statements:
1. A credit in a real account implies the value of the asset has decreased.
2. A debit in a nominal account signifies an income or profit.
3. A credit in a personal account implies the person has become a creditor.

Which of the statements are correct?
(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(C) 1 and 3 only
Statement 1 is correct as crediting a real account means the asset is going out or decreasing. Statement 3 is correct as crediting a personal account means the person is a giver, hence a creditor. Statement 2 is incorrect; a debit in a nominal account signifies an expense or a loss, not an income or profit.

May/June 2023

102. What is the correct sequence of steps for balancing a ledger account?
1. Bring down the balance on the opposite side

for the next period.
2. Total the amounts of debit and credit entries.
3. Put the difference on the side where the amount is short, writing 'To Balance c/d' or 'By Balance c/d'.

(A) 1, 2, 3
(B) 2, 3, 1
(C) 3, 2, 1
(D) 2, 1, 3

Ans :

(B) 2, 3, 1
The correct procedure for balancing an account is to first total both the debit and credit sides (Step 2). Then, calculate the difference and write it on the shorter side as 'Balance c/d' to make the totals equal (Step 3). Finally, this balance is brought down ('Balance b/d') to the opposite side to start the next accounting period (Step 1).

Oct/Nov 2018

103. Which of the following is NOT an advantage of the Imprest System of Petty Cash?
(A) It allows the petty cashier to draw cash from the chief cashier whenever desired.
(B) It helps in minimizing the chances of defalcation of cash.
(C) It ensures that petty cash accounts are always kept up to date.
(D) It relieves the chief cashier from the task of recording numerous small payments.

Ans :

(A) It allows the petty cashier to draw cash from the chief cashier whenever desired.
This statement describes a disadvantage that the imprest system is designed to prevent. A key feature of the system is control; the petty cashier cannot draw cash at will. They are given a fixed float and are only reimbursed for actual expenditure after submitting accounts, which restricts ad-hoc withdrawals and enhances control.

May/June 2007

104. "The term 'posting' means transferring the debit and credit items from the journal to their respective accounts in the ledger...The concerned account that has been debited in the journal should also be debited in the ledger...a reference should be made of the other account that has been credited in the journal."
Based on this, if the journal entry is "Salaries a/c Dr. 5,000; To Cash a/c 5,000", how is it posted to the Salaries Account?
(A) On the credit side, as 'By Cash a/c' ₹5,000.
(B) On the debit side, as 'To Salaries a/c' ₹5,000.
(C) On the credit side, as 'By Salaries a/c' ₹5,000.
(D) On the debit side, as 'To Cash a/c' ₹5,000.

Ans :

(D) On the debit side, as 'To Cash a/c' ₹5,000.
The journal entry debits the Salaries Account. As per the rule, the posting must also be on the debit side of the Salaries Account. The reference should be to the other account involved in the entry, which is the Cash Account. The convention is to use 'To' on the debit side. Thus, the entry is 'To Cash a/c' for ₹5,000.

Oct/Nov 2025

105. A transaction states: "Purchased goods from Suresh ₹2,000". How should this be interpreted for journalising?
(A) As a credit transaction, because the name of the party is given and there is no mention of cash.
(B) As a cash transaction, because the amount is small.
(C) As a cash transaction, because the word 'paid' is implied.
(D) As a purchase of an asset, debiting the Asset account.

Ans :

(A) As a credit transaction, because the name of the party is given and there is no mention of cash.
According to accounting conventions for journalising, when the name of the party (Suresh) is mentioned in a transaction and there is no explicit mention of 'cash', 'paid', or 'received', the transaction is assumed to be on a credit basis. Therefore, this is a credit purchase from Suresh, creating a liability.

May/June 2012

106. Which of the following items are recorded in a Columnar Petty Cash Book?
I. Purchase of postage stamps (₹10)
II. Purchase of machinery on credit (₹50,000)
III. Paid for conveyance to office clerk (₹25)
IV. Payment of salaries by cheque (₹20,000)
(A) I and II only
(B) I and III only
(C) II and IV only
(D) I, III and IV

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Ans :

(B) I and III only
The petty cash book is used exclusively for small cash payments. Purchase of postage stamps (₹10) and conveyance for a clerk (₹25) are classic examples of petty expenses. Purchase of machinery on credit and payment of salaries by cheque are major transactions that would be recorded in the general journal and the main cash book, respectively.

Oct/Nov 2014

107. "In practice, cash receipts and the cash payments book may be employed respectively to record the cash receipts and cash payments especially when the cash transactions are numerous. The posting is usually done daily from these books to the ledger accounts."
This describes the use of:
(A) A three-column cash book
(B) A petty cash book
(C) The general journal
(D) Separate journals for cash receipts and cash payments

Ans :

(D) Separate journals for cash receipts and cash payments
The excerpt describes a system where, instead of a single cash book, two separate books are maintained: one exclusively for all cash receipts (Cash Receipts Journal) and another for all cash payments (Cash Payments Journal). This is a method used by businesses with a high volume of transactions to divide the workload and specialize the recording process.

May/June 2019

108. Which statement correctly differentiates a simple petty cash book from a columnar petty cash book?
(A) In a simple book, each payment is posted individually to the ledger, while a columnar book allows for posting of totals.
(B) The simple book uses the imprest system, while the columnar book does not.
(C) The simple book is for large payments, and the columnar book is for small payments.
(D) The simple book has debit and credit sides, while the columnar book only has a credit side.

Ans :

(A) In a simple book, each payment is posted individually to the ledger, while a columnar book allows for posting of totals.
The main drawback of a simple petty cash book is that every single payment must be posted as a separate debit to its respective ledger account. The columnar petty cash book overcomes this by providing analysis columns for common expenses, whose totals can be posted to the ledger periodically, saving significant time and effort.

Oct/Nov 2006

109. What does the 'C.B.F.' column on the debit side of a simple petty cash book specimen stand for?
(A) Credit Balance Forward
(B) Carried Balance Forward
(C) Cash Book Folio
(D) Customer Balance File

Ans :

(C) Cash Book Folio
The 'C.B.F.' column on the debit (receipt) side of the petty cash book stands for Cash Book Folio. When the petty cashier receives cash from the chief cashier, the transaction is recorded on the credit side of the main cash book. The page number of the main cash book where this entry is made is recorded in the C.B.F. column for cross-reference.

May/June 2021

110. A business has a two-column cash book. It receives a cheque for ₹950 from a customer in full settlement of a debt of ₹1,000. How is this recorded?
(A) Debit Cash ₹950, Debit Discount ₹50
(B) Debit Bank ₹950, Debit Discount ₹50
(C) Debit Cash ₹1,000
(D) Debit Cash ₹950, Credit Discount ₹50

Ans :

(A) Debit Cash ₹950, Debit Discount ₹50
In a two-column cash book with cash and discount columns, the amount of money actually received (₹950) is recorded in the Cash column on the debit side. The discount of ₹50 (₹1,000 - ₹950) given to the customer is a 'discount allowed', which is an expense for the business. It is recorded in the Discount column, also on the debit side.

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Oct/Nov 2010

111. Consider the following statements about a three-column cash book:

1. It eliminates the need for a separate bank account in the ledger.
2. The discount column is a memorandum column and is not balanced.
3. A withdrawal of cash from the bank for personal use is a contra entry.
4. The bank column operates on the rules of a real account.

Which of the above statements are correct?

(A) 1 and 2 only
(B) 1, 2, and 3 only
(C) 2 and 4 only
(D) All of the above

Ans :

(A) 1 and 2 only
Statements 1 and 2 are correct. The three-column cash book includes a bank column that functions as the bank account, and the discount columns are memorandum. Statement 3 is incorrect; withdrawal for personal use is 'Drawings', not a contra entry. Statement 4 is incorrect; the bank column represents a personal account, not a real account.

May/June 2005

112. When goods are returned to a supplier, the term used is 'Purchases Return' or:

(A) Returns Inward
(B) Returns Outward
(C) Sales Return
(D) Goods Returned

Ans :

(B) Returns Outward
When a business returns goods that it had previously purchased, the transaction is recorded as a 'Purchases Return'. Since the goods are going out of the business back to the supplier, this is also known as 'Returns Outward'. This is distinct from 'Returns Inward' or 'Sales Return', which refers to goods returned by customers.

Oct/Nov 2022

113. Based on the definition, "In order to obtain the details of an item, the business transactions are recorded in accounts...An account is an individual record of a person, firm, or thing, an item of income or an expense," which of the following would NOT be considered an account?

(A) Cash
(B) Mr. Prasad
(C) The entire business enterprise
(D) Salaries

Ans :

(C) The entire business enterprise
An account is a specific record for an individual item like cash (thing), Mr. Prasad (person), or salaries (expense). The entire business enterprise is the entity for which the accounts are being kept; it is not an account itself. The enterprise is composed of numerous individual accounts that collectively reflect its financial position and performance.

May/June 2018

114. **Assertion (A) :** The journal is more reliable as compared to the ledger.
Reason (R) : The journal is the book in which the entry is passed first, providing a complete chronological record of the transaction.

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
The journal is considered more reliable because it is the book of prime entry. Transactions are recorded here first, in full, with a narration explaining the event. The ledger only contains classified parts of these entries. The primary, complete, and chronological nature of the journal record is the basis for its higher reliability in case of a dispute or error.

Oct/Nov 2016

115. Identify the correct statement regarding the balancing of accounts.

(A) If the debit and credit sides are equal, the account has a zero balance and is considered open.
(B) A debit balance is brought down on the credit side of the account for the next period.
(C) The process involves equalising the two sides by putting the difference on the side that is short.
(D) Nominal accounts are balanced at the end of

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the year using 'By Balance c/d'.

Ans :

(C) The process involves equalising the two sides by putting the difference on the side that is short. Balancing an account is the mechanical process of making the debit and credit totals equal. This is achieved by calculating the difference between the two sides and inserting this difference on the side with the smaller total. This balancing figure is labeled 'Balance c/d' (carried down), after which the totals on both sides will match.

May/June 2014

116. In Illustration 10, Kesari purchased 20 shares of ABC Ltd. at ₹20 per share. What is the journal entry to record this?
(A) ABC Ltd. a/c Dr. 400; To Cash a/c 400
(B) Investments a/c Dr. 400; To Cash a/c 400
(C) Purchases a/c Dr. 400; To Cash a/c 400
(D) Drawings a/c Dr. 400; To Cash a/c 400

Ans :

(B) Investments a/c Dr. 400; To Cash a/c 400
The purchase of shares is not a purchase of 'goods' for resale, so the Purchases account is not used. Shares are bought as an investment to earn returns. Therefore, an asset account 'Investments a/c' is debited to record the acquisition of the asset (20 shares × ₹20/share = ₹400). Cash is paid, so Cash a/c is credited.

Oct/Nov 2007

117. Which of the following transactions would be recorded in the general journal and not in a specialized journal like a cash book or purchases book?
(A) Sale of goods for cash.
(B) Purchase of goods on credit.
(C) Purchase of office equipment on credit.
(D) Payment of rent in cash.

Ans :

(C) Purchase of office equipment on credit.
Sale of goods for cash and payment of rent go to the cash book. Purchase of goods on credit goes to the purchases book. The purchase of an asset (office equipment) on credit is a non-cash, non-goods purchase transaction. Since it doesn't fit into any of the common specialized journals, it is recorded in the general journal.

May/June 2025

118. What is the correct treatment for the transaction "Paid carriage and cartage on goods sold to Mr. Nayan on his behalf ₹40"?
(A) Mr. Nayan a/c, Credit Cash a/c.
(B) Debit Carriage a/c, Credit Cash a/c.
(C) Debit Sales a/c, Credit Cash a/c.
(D) Debit Cash a/c, Credit Mr. Nayan a/c.

Ans :

(A) Mr. Nayan a/c, Credit Cash a/c.
The expense was paid 'on behalf of' Mr. Nayan. This means the expense is Mr. Nayan's responsibility, but the business paid it for him. The business will recover this amount from him. Therefore, Mr. Nayan's account (debtor) is debited to increase the amount he owes. Cash a/c is credited because cash was paid by the business.

Oct/Nov 2019

119. A firm pays ₹1,220 for salaries and ₹180 for advertising. The compound journal entry would be:
(A) Cash a/c Dr. 1,400; To Salaries a/c 1,220; To Advertising a/c 180.
(B) Expenses a/c Dr. 1,400; To Cash a/c 1,400.
(C) Salaries a/c Dr. 1,220; Advertising a/c Dr. 180; To Cash a/c 1,400.
(D) Salaries a/c Dr. 1,220; To Advertising a/c 180; To Cash a/c 1,040.

Ans :

(C) Salaries a/c Dr. 1,220; Advertising a/c Dr. 180; To Cash a/c 1,400.
A compound entry is used to record this transaction. Both salaries and advertising are expenses, so their respective nominal accounts are debited. The total cash paid is the sum of both expenses (₹1,220 + ₹180 = ₹1,400). As cash is going out, the Cash account is credited with the total amount of ₹1,400.

May/June 2009

120. Match List-I (Book/Process) with List-II (Description).

	List I		**List II**
P.	Journalising	1.	Book of final entry
Q.	Posting	2.	Process of recording in the journal
R.	Ledger	3.	Chronological record

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S.	Journal	4.	Transferring from journal to ledger

Code:
(A) P-2, Q-4, R-1, S-3
(B) P-3, Q-1, R-4, S-2
(C) P-2, Q-1, R-4, S-3
(D) P-4, Q-2, R-3, S-1

Ans :

(A) P-2, Q-4, R-1, S-3
Journalising (P) is the process of recording in the journal (2). Posting (Q) is the process of transferring entries from the journal to the ledger (4). The Ledger (R) is known as the book of final entry or principal book (1). The Journal (S) is the book of primary entry where transactions are recorded chronologically (3).

Oct/Nov 2011

121. Consider the following statements:
Statement I : A bank account is an example of an artificial personal account.
Statement II : A bank account is an example of a real account.
Statement III: Goodwill is an example of a tangible real account.
Statement IV: Prepaid rent is an example of a representative personal account.
Which combination of statements is correct?
(A) I and III
(B) II and IV
(C) I and IV
(D) II and III

Ans :

(C) I and IV
Statement I is correct; a bank account represents the banking institution, an artificial person. Statement IV is correct; prepaid rent represents the landlord to whom payment has been made in advance, hence it is a representative personal account. Statement II is incorrect. Statement III is incorrect; goodwill is an intangible real account.

May/June 2010

122. Which of the following is an example of a transaction that would result in a Contra Entry?
(A) Payment to a creditor by cheque.
(B) Withdrawal of cash from bank for office use.
(C) Sale of goods for cash.
(D) Purchase of furniture on credit.

Ans :

(B) Withdrawal of cash from bank for office use.
A contra entry involves both the cash and bank accounts. Withdrawing cash from the bank for office use increases the business's cash in hand (debit cash column) and decreases the bank balance (credit bank column). Both aspects are recorded within the three-column cash book, making it a contra entry.

Oct/Nov 2024

123. From Illustration 7, the petty cashier received ₹200 on Nov 1. By Nov 15, total expenses were: Postage ₹10, Conveyance ₹25, Office Files ₹30, Cold Drinks ₹24, Regd. AD ₹18, Ramesh ₹50, Washing ₹10. What is the total expenditure and closing balance?
(A) Expenditure ₹177, Closing Balance ₹23
(B) Expenditure -₹200, Closing Balance ₹0
(C) Expenditure ₹167, Closing Balance ₹33
(D) Expenditure ₹157, Closing Balance ₹43

Ans :

(C) Expenditure ₹167, Closing Balance ₹33
The total expenditure is the sum of all payments: ₹10 + ₹25 + ₹30 + ₹24 + ₹18 + ₹50 + ₹10 = ₹167. The closing balance is the initial amount received minus the total expenditure: ₹200 - ₹167 = ₹33. This is the amount of cash the petty cashier has left at the end of the period.

May/June 2017

124. If a debit balance in a real account is a property, and a debit balance in a personal account is a debtor, what does a debit balance in a nominal account represent?
(A) An income or gain
(B) A liability
(C) A property
(D) An expense or loss

Ans :

(D) An expense or loss
The nature of a balance depends on the type of account. For nominal accounts, the rule is "Debit all expenses and losses." Therefore, a debit balance in an account like 'Rent Account' or 'Salaries Account' signifies an expense incurred by the business or a loss it has suffered during the accounting period.

Oct/Nov 2005

125. The equality of debits and credits in a journal entry must be established for:

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(A) All journal entries, whether simple or compound
(B) Simple entries only
(C) Compound entries only
(D) Opening entries only

Ans :

(A) All journal entries, whether simple or compound
The principle of duality is fundamental to the double-entry system. For every journal entry passed, regardless of whether it is a simple entry (one debit, one credit) or a compound entry (multiple debits/credits), the aggregate amount of debits must be exactly equal to the aggregate amount of credits. This ensures the accounting equation remains balanced.

May/June 2020

126. Consider the following four statements:
1. The journal is a book for analytical record.
2. The ledger is a book for chronological record.
3. The process of recording in the ledger is called 'posting'.
4. 'Journalising' is the process of recording transactions in the journal.

Which of the above are correct?
(A) 1 and 2
(B) 3 and 4
(C) 1 and 3
(D) 2 and 4

Ans :

(B) 3 and 4
Statement 3 is correct; 'posting' refers to transferring entries to the ledger. Statement 4 is also correct; 'journalising' is the act of recording in the journal. Statements 1 and 2 are incorrect; the journal is for chronological record, and the ledger is for analytical record. The roles are reversed in the statements.

Oct/Nov 2015

127. If a business receives ₹290 from Payal after allowing her a discount of ₹10, how is this recorded in a double-column cash book?
(A) Debit Cash ₹300.
(B) Debit Cash ₹290, Credit Discount ₹10.
(C) Debit Cash ₹290, no entry for discount.
(D) Debit Cash ₹290, Debit Discount ₹10.

Ans :

(D) Debit Cash ₹290, Debit Discount ₹10.
The cash actually received is ₹290, so the cash column on the debit side is debited with this amount. The discount of ₹10 is a 'discount allowed', which is an expense for the business. It is recorded in the discount column on the debit (receipts) side of the cash book.

May/June 2013

128. An account has a debit total of ₹15,000 and a credit total of ₹11,000. The account has a:
(A) Debit balance of ₹4,000
(B) Credit balance of ₹4,000
(C) Debit balance of ₹26,000
(D) Credit balance of ₹26,000

Ans :

(A) Debit balance of ₹4,000
A balance is the difference between the totals of the two sides. The debit side (₹15,000) is larger than the credit side (₹11,000). The difference is ₹4,000. Since the debit side is larger, the account is said to have a debit balance of ₹4,000. This balance would be written on the credit side as 'By Balance c/d' to equalize the totals.

Oct/Nov 2021

129. In the books of Kesari, Ambar's account had a debit balance of ₹1,200. On Feb 22, cash of ₹600 was received as he became insolvent. What is the compound journal entry to close Ambar's account?
(A) Cash a/c Dr. 600; To Ambar a/c 600.
(B) Ambar a/c Dr. 1,200; To Cash a/c 600; To Bad Debts a/c 600.
(C) Cash a/c Dr. 600; Bad Debts a/c Dr. 600; To Ambar a/c 1,200.
(D) Bad Debts a/c Dr. 1,200; To Ambar a/c 1,200.

Ans :

(C) Cash a/c Dr. 600; Bad Debts a/c Dr. 600; To Ambar a/c 1,200.
Cash is received, so Cash a/c is debited with ₹600. The unrecoverable amount of ₹600 is a loss, so Bad Debts a/c is debited with ₹600. Ambar's account, which had a debit balance, must be fully credited to close it, so it is credited with the total due amount of ₹1,200.

May/June 2024

130. **Assertion (A) :** The bank column in a three-column cash book always shows a debit balance.
Reason (R) : A business can withdraw more money from its bank account than its available

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balance, creating an overdraft.

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).

(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).

(C) (A) is true but (R) is false.

(D) (A) is false but (R) is true.

Ans :

(D) (A) is false but (R) is true.

Assertion (A) is false. Unlike the cash column, the bank column can show a credit balance, which represents a bank overdraft (a liability). Reason (R) is true; businesses with overdraft facilities can withdraw more money than their account balance. This possibility of an overdraft is precisely why the assertion is false.

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CHAPTER 4

Bank Reconciliation Statement

Oct/Nov 2015

1. According to the primary objectives of preparing a Bank Reconciliation Statement (BRS), which of the following is a key outcome for a business?

(A) To create a new, separate ledger specifically for all bank transactions.

(B) To identify and list the causes of differences between the cash book and pass book balances.

(C) To provide formal authorization for the bank to make payments to third parties.

(D) To formally apply for and secure an overdraft facility from the bank.

Ans :

(B) To identify and list the causes of differences between the cash book and pass book balances.

A primary objective of preparing a Bank Reconciliation Statement is to systematically identify, list, and describe the specific reasons for any discrepancy between the balance shown in the firm's cash book (bank column) and the balance shown in the bank's pass book or statement for the same period, ensuring financial accuracy.

May/June 2010

2. In modern business practice, why is a firm's bank operating account often treated like cash available with the firm?

(A) Because the funds in the account are highly liquid and can be withdrawn on demand.

(B) Because the bank is required to provide daily statements for tracking all transactions.

(C) Because all payments made from the account are legally guaranteed by the banking institution.

(D) Because the balance typically earns a high rate of interest comparable to a short-term investment.

Ans :

(A) Because the funds in the account are highly liquid and can be withdrawn on demand.

A firm's operating account balance is considered highly liquid and is treated like available cash because the funds can be accessed and withdrawn by the firm at any time to meet its payment obligations. This on-demand availability makes it a direct substitute for physical cash for operational purposes, facilitating transactions through cheques and electronic means.

Oct/Nov 2022

3. What is the purpose of adding a 'Bank' column to the traditional 'Cash' column in a cash book?

(A) To record only the transactions involving foreign currency.

(B) To track the personal banking transactions of the business owner.

(C) To account for all transactions taking place through the firm's bank account.

(D) To manage petty cash expenses separately from major expenditures.

Ans :

(C) To account for all transactions taking place through the firm's bank account.

A dedicated 'Bank' column is included in the cash book to specifically record all receipts and payments that are routed through the firm's bank account. This allows for a clear and separate tracking of bank transactions, distinguishing them from physical cash transactions, which are recorded in the 'Cash' column of the same book.

May/June 2016

4. Based on the principles of accounting, what is the correct journal entry in the cash book when a cheque is deposited into the bank?

(A) The bank account is credited, and the cash account is debited.

(B) The bank account is debited, and the account of the party issuing the cheque is credited.

(C) The bank account is posted with a Credit entry.

(D) The bank account is posted with a Debit entry.

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Ans :

(D) The bank account is posted with a Debit entry.
When a cheque is deposited into the bank, the bank is the receiver of the funds on behalf of the firm. According to the principle 'Debit the receiver', the bank account in the firm's cash book is debited. This entry signifies an increase in the firm's assets held at the bank, reflecting the inflow of funds.

Oct/Nov 2009

5. When a firm issues a cheque to a supplier, how is this transaction recorded in the bank column of its cash book?
(A) It is recorded as a debit entry, as it represents an increase in assets.
(B) It is not recorded until the cheque is presented for payment.
(C) It is recorded as a credit entry, as the bank is the giver of funds.
(D) It is recorded in both the debit and credit columns to balance the entry.

Ans :

(C) It is recorded as a credit entry, as the bank is the giver of funds.
When a firm issues a cheque, it is instructing its bank to pay a certain amount to a third party. In this context, the bank acts as the 'giver' of funds on behalf of the firm. Following the accounting principle 'Credit the giver', the transaction is recorded as a credit entry in the bank column of the cash book.

May/June 2023

6. What does a bank typically issue periodically to a firm, which serves as a statement of account for its transactions?
(A) A ledger book.
(B) A passbook or bank statement.
(C) A reconciliation certificate.
(D) A credit advice note.

Ans :

(B) A passbook or bank statement.
A bank periodically provides its customers with a passbook or a bank statement. This document is a copy of the customer's account as it appears in the bank's ledger, detailing all deposits, withdrawals, and other transactions that have affected the account balance over a specific period, providing an official record from the bank's perspective.

Oct/Nov 2018

7. In the context of a firm's passbook, how does the bank record a cash deposit of ₹ 10,000 made by the firm?
(A) As a debit entry of ₹ 10,000, reducing the firm's balance.
(B) As a debit entry of ₹ 10,000 in the firm's cash book.
(C) As a contra entry with an equal debit and credit, having no net effect on the balance.
(D) As a credit entry of ₹ 10,000, increasing the firm's balance.

Ans :

(D) As a credit entry of ₹ 10,000, increasing the firm's balance.
When a firm deposits cash into its bank account, the bank's liability to the firm increases. From the bank's perspective, the firm is a creditor. Therefore, the bank credits the firm's account to reflect this increased liability. This credit entry in the passbook corresponds to a debit entry in the firm's cash book for the same transaction.

May/June 2007

8. Why is a passbook often described as a 'mirror image' of the bank column of a cash book?
(A) Because a debit entry in the cash book is shown as a credit entry in the passbook, and vice versa.
(B) Because both documents are prepared by the firm's accountant.
(C) Because the transaction dates in both the cash book and passbook are always identical.
(D) Because both documents show the same closing balance at all times.

Ans :

(A) Because a debit entry in the cash book is shown as a credit entry in the passbook, and vice versa.
The passbook is considered a mirror image of the cash book's bank column because the accounting perspectives are opposite. A deposit, which increases the firm's asset (debit in cash book), increases the bank's liability (credit in passbook). Conversely, a withdrawal decreases the firm's asset (credit in cash book) and decreases the bank's liability (debit in passbook).

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Oct/Nov 2025

9. What does a debit balance in the cash book's bank column represent, and how is it reflected in the passbook?
(A) It represents an overdraft and is reflected as a debit balance in the passbook.
(B) It represents a favourable balance and is reflected as a debit balance in the passbook.
(C) It represents a favourable balance and is reflected as a credit balance in the passbook.
(D) It represents an overdraft and is reflected as a credit balance in the passbook.

Ans :

(C) It represents a favourable balance and is reflected as a credit balance in the passbook.
A debit balance in the cash book's bank column indicates that the firm has a positive or favourable amount of funds in its bank account. This same balance is shown as a credit balance in the passbook because, from the bank's perspective, this amount is a liability owed to the customer, making the customer a creditor of the bank.

May/June 2012

10. A firm issues a cheque on June 15th, which is recorded immediately in its cash book. The bank pays the cheque on June 20th. This situation exemplifies a primary reason for differences between the cash book and passbook, which is:
(A) A delay in reflection or a timing difference.
(B) An error made by the firm's accountant.
(C) A direct deposit made by a customer.
(D) The bank charging service fees.

Ans :

(A) A delay in reflection or a timing difference.
The discrepancy arises because the firm records the transaction on the date the cheque is issued, while the bank only records it when the cheque is presented and paid. This time lag between the two recording dates is a common cause for temporary differences between the cash book balance and the passbook balance, known as a timing difference.

Oct/Nov 2014

11. Which of the following is classified as an 'Error' that can cause a discrepancy between the cash book and passbook balances?
(A) A cheque issued by the firm but not yet presented for payment.
(B) Bank charges debited by the bank but not yet recorded by the firm.
(C) A cheque deposited but not yet cleared by the bank.
(D) Undercasting the total of the payments side of the cash book.

Ans :

(D) Undercasting the total of the payments side of the cash book.
Undercasting (incorrectly totaling to a lower amount) the payments side of the cash book is a clerical error made by the accountant. This mistake leads to an artificially inflated cash book balance compared to the actual position, causing a discrepancy with the passbook balance. The other options represent timing differences, not accounting errors.

May/June 2019

12. Which of the following is an example of an entry that appears first in the cash book and later in the pass book, causing a temporary difference?
(A) Interest credited by the bank on the account balance.
(B) A cheque deposited by the firm into the bank but not yet collected.
(C) Bank charges for issuing a new cheque book.
(D) A direct payment made into the account by a customer.

Ans :

(B) A cheque deposited by the firm into the bank but not yet collected.
When a firm deposits a cheque, it immediately debits its cash book. However, the bank will only credit the firm's account after the cheque is cleared through the clearing house. This time lag means the entry appears in the cash book first and is reflected in the pass book at a later date.

Oct/Nov 2006

13. A trader issues a cheque to a creditor on March 28th. The creditor presents the cheque to the bank for payment on April 4th. This transaction falls under which category of causes for BRS differences?
(A) Entries which Require Change in Cashbook.
(B) Errors in the passbook.
(C) Cheques Issued but not Presented for Payment.
(D) Direct payments into the bank.

Ans :

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(C) Cheques Issued but not Presented for Payment.
This is a classic timing difference where the trader records the payment in March, but the bank processes it in April. As of March 31st, this would be classified as a 'Cheque Issued but not Presented for Payment'. This type of entry appears first in the cash book and later in the pass book.

May/June 2021

14. Identify the statement that correctly describes 'Cheques Deposited into Bank but not yet Collected'.
(A) The trader credits the cash book, but the bank has not yet credited the passbook.
(B) The trader debits the cash book, and the bank immediately credits the passbook.
(C) The trader credits the cash book, but the bank has not yet debited the passbook.
(D) The trader debits the cash book, but the bank has not yet credited the passbook.

Ans :

(D) The trader debits the cash book, but the bank has not yet credited the passbook.
When cheques are received and deposited, the trader makes an immediate entry on the debit (receipts) side of the cash book. The bank, however, only credits the customer's account after the cheque is cleared. The time lag between deposit and clearance results in this reconciling item, which does not require a change in the cashbook.

Oct/Nov 2010

15. Which of the following transactions originates in the pass book first and subsequently requires an entry in the cash book?
(A) Bank charges debited by the bank for services rendered.
(B) A cheque issued to a supplier for goods purchased.
(C) A cheque received from a customer and deposited into the bank.
(D) A cash withdrawal made from the bank for office use.

Ans :

(A) Bank charges debited by the bank for services rendered.
Bank charges are levied directly by the bank and are first recorded as a debit in the customer's pass book. The trader typically becomes aware of these charges upon receiving the bank statement or an advice, and only then makes the corresponding credit entry in the cash book to account for the expense.

May/June 2005

16. When a bank credits a customer's account for interest earned on a savings balance, how should the trader account for this transaction?
(A) The trader should make a credit entry on the payments side of the cash book.
(B) The trader should make a debit entry on the receipts side of the cash book.
(C) No entry is required in the cash book as it is an automatic bank transaction.
(D) The trader should inform the bank to reverse the entry.

Ans :

(B) The trader should make a debit entry on the receipts side of the cash book.
Interest credited by the bank represents income for the trader and an increase in the bank balance. To reflect this, the trader must make a debit entry in the bank column on the receipts side of the cash book after learning about the credit from the pass book or bank advice, thus updating the cash book.

May/June 2018

17. A trader has an overdraft facility. The bank charges interest on the overdrawn balance. This transaction will first appear as:
(A) A credit entry in the pass book.
(B) A debit entry in the pass book.
(C) A debit entry in the cash book.
(D) A credit entry in the cash book.

Ans :

(B) A debit entry in the pass book.
Interest on an overdraft is an expense for the trader and reduces the amount available in the account (or increases the overdraft). The bank will directly debit the customer's account to charge this interest. This debit entry appears first in the pass book, and the trader records it later in the cash book.

Oct/Nov 2016

18. If a trader has given a standing instruction to the bank to collect dividends on investments, where will this transaction be recorded first?
(A) On the debit side of the cash book.

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(B) On the credit side of the cash book.
(C) As a credit entry in the pass book.
(D) As a debit entry in the pass book.

Ans :

(C) As a credit entry in the pass book.
When the bank collects a dividend on behalf of the trader based on a standing instruction, it credits the amount to the trader's account. This entry appears first in the pass book. The trader will then make a corresponding debit entry in the cash book upon receiving the bank advice or reviewing the pass book.

May/June 2014

19. A firm instructs its bank via standing instruction to pay its annual life insurance premium of ₹ 15,000. How is this transaction reflected in the books?
(A) The bank first debits the pass book, and the firm later credits the cash book.
(B) The firm first credits the cash book, and the bank later debits the pass book.
(C) The bank first credits the pass book, and the firm later debits the cash book.
(D) The firm first debits the cash book, and the bank later credits the pass book.

Ans :

(A) The bank first debits the pass book, and the firm later credits the cash book.
For a payment based on a standing instruction, the bank acts first by debiting the firm's account on the due date. This reduces the bank balance and is recorded in the pass book. The firm updates its records by making a credit entry in its cash book after being notified by the bank.

Oct/Nov 2007

20. What is the accounting consequence of a direct deposit made by a customer into a firm's bank account?
(A) The passbook balance will be lower than the cash book balance until reconciled.
(B) The cash book balance will be lower than the passbook balance until reconciled.
(C) Both the passbook and cash book balances increase simultaneously.
(D) It is treated as an error and must be reversed by the bank.

Ans :

(B) The cash book balance will be lower than the passbook balance until reconciled.
A direct deposit by a customer is first credited by the bank, increasing the passbook balance. The firm is often unaware of this transaction until it checks its bank statement. Therefore, the cash book balance remains unchanged and lower than the passbook balance until the firm makes a corresponding debit entry.

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May/June 2025

21. When a cheque previously deposited by a trader is dishonoured, what action does the bank take?
(A) The bank issues a new cheque book to the trader.
(B) The bank waits for the trader's instruction before taking any action.
(C) The bank debits the customer's account for the amount of the dishonoured cheque.
(D) The bank credits the customer's account to reverse the initial deposit.

Ans :

(C) The bank debits the customer's account for the amount of the dishonoured cheque.
If a deposited cheque is dishonoured, the bank, which might have given provisional credit, will reverse the entry by debiting the customer's account. This action reduces the account balance by the cheque amount, and the trader must then make a corresponding credit entry in the cash book to reflect the dishonour.

Oct/Nov 2019

22. In the process of reconciliation, finding entries like 'cheques issued but not presented' helps in arriving at what figure?
(A) The adjusted (corrected) cashbook balance.
(B) The notional 'Adjusted bank balance'.
(C) The total clerical errors in the cashbook.
(D) The opening balance for the next period.

Ans :

(B) The notional 'Adjusted bank balance'.
The first step in reconciliation involves adjusting the passbook balance for items that are already in the cashbook but not yet in the passbook (e.g., unpresented cheques, uncleared deposits). This calculation results in a notional figure called the 'Adjusted bank balance', which is used for comparison, not for the final balance sheet.

May/June 2009

23. Which of the following steps in the reconciliation process results in an actual change to the cashbook balance that is carried forward to the trial balance?
(A) Finding out entries which do not require a change in the cashbook.
(B) Preparing a draft of the Bank Reconciliation Statement.
(C) Calculating the 'Adjusted bank balance'.
(D) Finding and posting entries present in the bank statement but not in the cashbook.

Ans :

(D) Finding and posting entries present in the bank statement but not in the cashbook.
Items like bank charges, interest credited, or direct deposits are first recorded by the bank. When these are discovered, the firm must update its cashbook by posting these missing entries. This process, along with correcting clerical errors, actually changes the cashbook balance to its correct, updated value which then appears in the trial balance.

Oct/Nov 2011

24. According to the standard format for preparing a Bank Reconciliation Statement, how are 'cheques deposited but not yet credited' treated when starting with the closing balance as per the bank statement?
(A) They are subtracted from the bank statement balance.
(B) They are added to the bank statement balance.
(C) They are ignored as they do not affect the bank balance.
(D) They are adjusted directly in the cashbook only.

Ans :

(B) They are added to the bank statement balance.
When starting with the bank statement balance, 'cheques deposited but not yet credited' are added. This is because these amounts have already been recorded as receipts (debited) in the cash book, increasing its balance. To reconcile, we must show what the bank balance would be if these deposits had been credited.

Oct/Nov 2024

25. When preparing a BRS starting from the balance as per the bank statement, how are 'cheques issued but not presented for payment' handled?
(A) They are added to the cashbook balance.
(B) They are ignored until they are presented.
(C) They are subtracted from the bank statement balance.
(D) They are added to the bank statement balance.

Ans :

(C) They are subtracted from the bank statement balance.
Cheques issued have already been credited in the cash book, reducing its balance. However, since they have not been presented, the bank statement balance is artificially high. To reconcile, this amount must be subtracted from the bank statement balance to reflect the outstanding payments that will eventually reduce the bank balance.

May/June 2017

26. In the BRS preparation format, which items are subtracted from the 'Balance as per cashbook' to arrive at the 'Adjusted (corrected) cashbook balance'?
(A) Credit entries shown in the bank statement but not appearing in the cashbook.
(B) Clerical errors that caused an under-debiting of the cashbook.
(C) Debit entries shown in the bank statement but not appearing in the cashbook.
(D) Cheques deposited but not yet credited by the bank.

Ans :

(C) Debit entries shown in the bank statement but not appearing in the cashbook.
Debit entries in the bank statement, such as bank charges or interest on overdraft, represent expenses or reductions in the bank balance that the firm has not yet recorded. To correct the cashbook, these amounts must be subtracted from the cashbook balance, bringing it to the true adjusted figure that reflects these transactions.

Oct/Nov 2005

27. What is the significance of the condition where the 'Adjusted balance in the bank statement' (A) is equal to the 'Adjusted (corrected) cashbook balance' (B)?

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(A) It indicates that the bank has made an error.
(B) It confirms that the balances have been successfully reconciled.
(C) It means no further entries are required in the next accounting period.
(D) It shows that the initial starting balances were identical.

Ans :

(B) It confirms that the balances have been successfully reconciled.
The entire purpose of the Bank Reconciliation Statement is to explain the difference between the two initial balances. When the adjusted bank balance (A) equals the adjusted cashbook balance (B), it signifies that all discrepancies have been accounted for through timing differences and necessary cashbook corrections, and the reconciliation is complete and correct.

May/June 2020

28. How should a debit balance in the bank statement (passbook) be treated for the purpose of arithmetical accuracy in a BRS?
(A) It should be treated as a negative figure representing an overdraft.
(B) It should be treated as a positive figure representing funds available.
(C) It should be ignored and the cash book balance should be used as the starting point.
(D) It should be added to the cash book credit balance.

Ans :

(A) It should be treated as a negative figure representing an overdraft.
A debit balance in a bank statement or passbook signifies that the account is overdrawn, meaning the customer owes money to the bank. For accurate arithmetical calculations within the Bank Reconciliation Statement, this overdraft balance must be treated as a negative figure, as it represents a liability for the customer rather than an asset.

May/June 2013

29. If a firm receives a cheque for ₹ 80,000 on June 30th and deposits it, but the bank only credits the amount after a 3-day clearing process, what is the primary need for bank reconciliation in this scenario?
(A) To ensure the bank does not lose the cheque.
(B) To allow the firm to issue cheques against the ₹ 80,000 immediately.
(C) To understand why the cash book balance and pass book balance do not tally on June 30th.
(D) To calculate the interest earned on the deposit.

Ans :

(C) To understand why the cash book balance and pass book balance do not tally on June 30th.
The firm records the ₹ 80,000 on June 30th, but the bank does not. This creates a timing difference and a discrepancy between the two balances. A BRS is necessary to systematically explain this difference and to know the actual cleared balance available, preventing the firm from overdrawing its account by issuing cheques against un-cleared funds.

Oct/Nov 2021

30. Which of the following is an example of a clerical error that would require an adjustment in the cash book during reconciliation?
(A) A debit balance of ₹ 1,526 being brought forward as a credit balance.
(B) Bank charges of ₹ 500 debited by the bank.
(C) A dividend of ₹ 1,000 collected by the bank on behalf of the trader.
(D) A cheque of ₹ 5,000 issued but not yet presented for payment.

Ans :

(A) A debit balance of ₹ 1,526 being brought forward as a credit balance.
Bringing forward a debit balance (asset) as a credit balance (liability) is a significant clerical error in bookkeeping. This mistake distorts the cash book balance and must be corrected within the cash book itself. The other options represent items omitted from the cash book or timing differences, not direct clerical errors in posting.

May/June 2024

31. Given that for Mr. G, total cheques drawn were ₹ 11,514, but only ₹ 7,815 were encashed, what is the total value of 'cheques issued but not presented for payment' as of 31st December 2022?
(A) ₹ 3,699
(B) ₹ 11,514
(C) ₹ 7,815
(D) ₹ 19,329

Ans :

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(A) ₹ 3,699
The total value of cheques issued (drawn) during the last week of December was ₹ 11,514. Out of these, cheques worth ₹ 7,815 were encashed (presented and paid) by the bank. The difference, which is ₹ 11,514 - ₹ 7,815 = ₹ 3,699, represents the amount of cheques that were issued but not yet presented for payment.

Oct/Nov 2008

32. In a cash book, a debit balance of ₹ 1,526 was brought forward as a credit balance. How does this error affect the cash book?
(A) It understates the cash book balance by ₹ 1,526.
(B) It understates the cash book balance by ₹ 3,052.
(C) It overstates the cash book balance by ₹ 1,526.
(D) It overstates the cash book balance by ₹ 3,052.

Ans :

(B) It understates the cash book balance by ₹ 3,052.
A debit balance of ₹ 1,526 is an asset. By recording it as a credit balance, it is treated as a liability of ₹ 1,526. The total error is the sum of the amount that should have been added and the amount that was wrongly subtracted, which is ₹ 1,526 + ₹ 1,526 = ₹ 3,052. The cash book is understated by this amount.

May/June 2006

33. If a bank collected a dividend of ₹ 250 and paid a subscription of ₹ 100 on behalf of Mr. G, and neither transaction was in the cash book, what is the net adjustment required in the cash book?
(A) A net credit of ₹ 150.
(B) A net debit of ₹ 350.
(C) A net debit of ₹ 150.
(D) A net credit of ₹ 350.

Ans :

(C) A net debit of ₹ 150.
The dividend of ₹ 250 collected by the bank is an income and should be debited to the cash book. The subscription of ₹ 100 paid by the bank is an expense and should be credited. The net effect is a debit of ₹ 250 and a credit of ₹ 100, resulting in a net increase, or net debit, of ₹ 150.

Oct/Nov 2017

34. Given the following clerical errors in Mr. G's cash book: 1. Payments side was undercast by ₹ 100. 2. A cheque for ₹ 131 issued was not recorded in the bank column. 3. A deposit of ₹ 150 was wrongly recorded in the cash column. 4. A debit balance of ₹ 1,526 was brought forward as a credit balance. 5. An outgoing cheque of ₹ 350 was recorded twice. What is the total net debit adjustment to be made?
(A) ₹ 3,552
(B) ₹ 231
(C) ₹ 3,782
(D) ₹ 3,321

Ans :

(D) ₹ 3,321
The errors requiring correction are: deposit not in bank column (+₹150 Dr), wrong carry forward (+₹3,052 Dr), outgoing cheque recorded twice (+₹350 Dr), undercasting payment side (-₹100 Dr or +₹100 Cr), and cheque issued not recorded (-₹131 Cr). The net debit is (₹150 + ₹3,052 + ₹350) - (₹100 + ₹131) = ₹3,552 - ₹231 = ₹3,321.

May/June 2008

35. Mr. G's pass book shows a balance of ₹ 15,534. Total cheques drawn were ₹ 11,514, of which ₹ 7,815 were encashed. Assuming no other timing differences, what is the 'Adjusted balance in the bank statement'?
(A) ₹ 19,233
(B) ₹ 8,364
(C) ₹ 11,835
(D) ₹ 15,534

Ans :

(C) ₹ 11,835
Starting with the pass book balance of ₹ 15,534, the adjustment for timing differences is for cheques issued but not presented. This amount is ₹ 11,514 - ₹ 7,815 = ₹ 3,699. This must be subtracted from the pass book balance. Therefore, the adjusted bank balance is ₹ 15,534 - ₹ 3,699 = ₹ 11,835. This is the notional reconciled balance.

Oct/Nov 2013

36. Given a Bank Reconciliation Statement extract: Balance as per cashbook: ₹ 8,364; Add: Clerical errors: ₹ 3,321; Add: Credit entries shown in the bank statement but not appearing in cashbook: ₹ 250; Subtract: Debit entries shown in the bank statement but not appearing in cashbook: ₹ 100; Adjusted (corrected) cashbook balance: ₹ 11,835. Based on this extract, what was the original uncorrected cash book balance?

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(A) ₹ 11,835
(B) ₹ 8,364
(C) ₹ 3,321
(D) ₹ 15,534

Ans :

(B) ₹ 8,364
The calculation clearly begins with the line "Balance as per cashbook" and states the figure as ₹ 8,364. This represents the starting point, which is the unadjusted balance recorded in the firm's books before the reconciliation process identified and incorporated the necessary corrections for errors and omissions from the bank statement.

May/June 2015

37. Given a Bank Reconciliation Statement extract, the adjustment 'Add: Credit entries shown in the bank statement but not appearing in cashbook: ₹ 250' most likely refers to which transaction?
(A) A cheque deposited by the firm but not yet cleared.
(B) An error where a payment was overstated in the cash book.
(C) A cheque issued by the firm but not yet paid by the bank.
(D) A direct deposit by a customer or dividend collected by the bank.

Ans :

(D) A direct deposit by a customer or dividend collected by the bank.
A credit entry in the bank statement that is not in the cash book represents an inflow of funds that the firm was unaware of. Examples include dividends collected by the bank on the firm's behalf or a customer depositing money directly into the account. These items increase the bank balance and must be added to the cash book.

Oct/Nov 2012

38. Given a Bank Reconciliation Statement extract, the adjustment 'Subtract: Debit entries shown in the bank statement but not appearing in cashbook: ₹ 100' typically represents what kind of transaction?
(A) Bank charges or a payment made by the bank on standing instruction.
(B) A dishonoured cheque.
(C) An overcasting of the receipts side of the cash book.
(D) A cash withdrawal recorded only in the cash book.

Ans :

(A) Bank charges or a payment made by the bank on standing instruction.
A debit entry in the bank statement not found in the cash book indicates an outflow of funds initiated by the bank. Common examples are bank service charges, interest on an overdraft, or payments like insurance premiums made based on standing instructions. These must be subtracted to correct the cash book balance.

May/June 2011

39. What is the primary characteristic of an overdraft balance as per the pass book when used in a BRS calculation?
(A) It is treated as a positive figure and added to cheques deposited.
(B) It is ignored, and the calculation starts from zero.
(C) It is shown as a negative figure.
(D) It must be equal to the cash book's debit balance.

Ans :

(C) It is shown as a negative figure.
An overdraft balance in the pass book signifies that the account holder owes money to the bank, representing a liability for the holder. In the arithmetical process of preparing a BRS, this balance is correctly represented as a negative figure to ensure that additions and subtractions accurately reflect the financial position of the account.

Oct/Nov 2020

40. A firm's cash book shows a credit balance of ₹ 12,300. How should this be interpreted and treated in a BRS?
(A) As an overdraft, treated as a negative figure.
(B) As a favourable balance, treated as a positive figure.
(C) As a clerical error that needs to be reversed.
(D) As cash in hand, not relevant to the bank reconciliation.

Ans :

(A) As an overdraft, treated as a negative figure.
In a cash book's bank column, a debit balance is favourable (asset), while a credit balance indicates an overdraft (liability). Therefore, a credit balance of ₹ 12,300 signifies that the firm has overdrawn its account according to its own

NODIA

records. For BRS calculations, this should be treated as a negative amount.

May/June 2022

41. A firm issued cheques for ₹ 7,000, of which only ₹ 3,000 were encashed. What is the value of 'cheques issued but not presented' that should be used in the BRS for this firm?
(A) ₹ 7,000
(B) ₹ 3,000
(C) ₹ 10,000
(D) ₹ 4,000

Ans :

(D) ₹ 4,000
The total value of cheques issued by the firm was ₹ 7,000. Of this amount, cheques worth ₹ 3,000 were presented and encashed by the payees. The remaining amount, ₹ 7,000 - ₹ 3,000 = ₹ 4,000, represents the cheques that have been recorded as paid in the cash book but have not yet been debited by the bank.

Oct/Nov 2023

42. A firm deposited cheques for ₹ 3,500, of which only ₹ 500 were credited. What is the value of 'cheques deposited but not yet credited' to be included in the BRS?
(A) ₹ 3,500
(B) ₹ 3,000
(C) ₹ 500
(D) ₹ 4,000

Ans :

(B) ₹ 3,000
The firm deposited cheques amounting to a total of ₹ 3,500. However, the bank has only processed and credited cheques worth ₹ 500 to the account by the statement date. The difference, ₹ 3,500 - ₹ 500 = ₹ 3,000, is the amount of cheques that are still in the process of clearing and have not yet been credited.

Oct/Nov 2015

43. Given a pass book overdraft of ₹ 12,000, cheques deposited but not credited of ₹ 3,000, and cheques issued but not presented of ₹ 4,000, calculate the 'Adjusted balance in the bank statement'.
(A) A positive balance of ₹ 11,000.
(B) An overdraft of ₹ 11,000.
(C) An overdraft of ₹ 13,000.
(D) A positive balance of ₹ 13,000.

Ans :

(C) An overdraft of ₹ 13,000.
Start with the pass book overdraft (-₹ 12,000). Add cheques deposited but not yet credited (+₹ 3,000). Subtract cheques issued but not yet presented (-₹ 4,000). The calculation is (-12,000) + 3,000 - 4,000 = -₹ 13,000. This results in an adjusted bank overdraft balance of ₹ 13,000.

May/June 2010

44. In a given period, a bank collected ₹ 600 as interest and received a direct deposit of ₹ 400 from a debtor. Neither item was recorded in the firm's cash book. What is the total amount that needs to be added to the cash book balance for these items?
(A) ₹ 500
(B) ₹ 1,200
(C) ₹ 1,700
(D) ₹ 1,000

Ans :

(D) ₹ 1,000
The items credited by the bank but not yet in the cash book are the interest collection of ₹ 600 and the direct deposit from a debtor of ₹ 400. Both are receipts for the firm. The total amount to be added (debited) to the cash book is ₹ 600 + ₹ 400 = ₹ 1,000.

Oct/Nov 2022

45. A firm's cash book has a credit balance (overdraft) of ₹ 12,300. Unrecorded collections total ₹ 1,000, and unrecorded payments (overdraft interest and insurance premium) total ₹ 1,700. Calculate the 'Adjusted (corrected) cashbook balance'.
(A) A credit balance of ₹ 13,000.
(B) A debit balance of ₹ 13,000.
(C) A credit balance of ₹ 11,600.
(D) A credit balance of ₹ 14,000.

Ans :

(A) A credit balance of ₹ 13,000.
Start with the cash book credit balance (-₹ 12,300). Add the unrecorded collections (+₹ 1,000). Subtract the unrecorded payments (-₹ 1,700). The calculation is
(-12,300) + 1,000 - 1,700 = -₹ 13,000,
which is a corrected credit balance (overdraft) of ₹ 13,000.

May/June 2016

46. When preparing a BRS using extracts of the cash book and pass book for the same period (e.g., both

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for January), which entries should be considered for reconciliation?

(A) Only the entries that appear in both the cash book and the pass book.
(B) Only the uncommon entries that appear in one book but not the other.
(C) Only the opening and closing balances of both books.
(D) All entries from both the cash book and the pass book.

Ans :

(B) Only the uncommon entries that appear in one book but not the other.

When comparing extracts for the same period, the entries that appear in both books are considered 'ticked' or cleared and do not cause a difference in the closing balances. The reconciling items are the 'uncommon' entries—those present in the cash book but missing from the pass book, and vice versa.

Oct/Nov 2009

47. If a cash book abstract is for January and the corresponding pass book abstract is for February, which entries are relevant for reconciling the January 31st balance?

(A) All uncommon entries from the January cash book.
(B) All uncommon entries from the February pass book.
(C) Only the common entries that appear in both the January cash book and the February pass book.
(D) Only the entries from the first week of January and the last week of February.

Ans :

(C) Only the common entries that appear in both the January cash book and the February pass book.

When the periods are different, an entry appearing in the January cash book and also in the February pass book signifies a timing difference. For example, a cheque issued in January (credit in Jan cash book) that was paid in February (debit in Feb pass book) is an unpresented cheque as of Jan 31st.

May/June 2023

48. When comparing the cash book debit side with the pass book credit side, what are you looking for?

(A) Deposits made by the firm that have been credited by the bank.
(B) Payments made by the firm that have been processed by the bank.
(C) Bank charges and other debits made by the bank.
(D) Cheques issued by the firm that have not yet been presented.

Ans :

(A) Deposits made by the firm that have been credited by the bank.

The debit side of the cash book (bank column) records all deposits and receipts. The credit side of the pass book records all credits made by the bank, which also correspond to deposits and receipts. Comparing these two sides helps identify which deposits have been cleared and which are outstanding.

Oct/Nov 2018

49. To identify 'cheques issued but not yet presented', which sides of the cash book and pass book should be compared?

(A) Cash book debit side and pass book credit side.
(B) Cash book credit side and pass book credit side.
(C) Cash book credit side and pass book debit side.
(D) Cash book debit side and pass book debit side.

Ans :

(C) Cash book credit side and pass book debit side.

The credit side of the cash book records all cheques issued and payments made by the firm. The debit side of the pass book records all withdrawals and payments processed by the bank. By comparing these two sides, one can identify the cheques that have been issued by the firm but have not yet been debited from its account.

May/June 2007

50. **Assertion (A) :** Where the period of the cash book and pass book extracts is the same, uncommon entries will appear in the reconciliation statement.
Reason (R) : Uncommon entries represent transactions recorded by one party but not the other within the same period, thus causing the difference in balances.

(A) Both (A) and (R) are true and (R) is the

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correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
The assertion correctly states the rule for same-period reconciliation. The reason provides the precise logic for this rule: these uncommon entries are the very definition of timing differences and omissions (e.g., an unpresented cheque is in the cash book but not the pass book), which are the items that a BRS is designed to identify and reconcile.

Oct/Nov 2025

51. Based on the following extracts for S Trading Company for December 2022: Cash Book shows a debit 'To Sheela' ₹ 10,500 (Dec 29). Bank Pass Book does not show a corresponding credit in December. Which cheque deposited by S Trading Company appears to be uncredited by the bank as of Dec 31st?
(A) Cheque from Vidya for ₹ 8,000.
(B) Cheque from Mamta for ₹ 3,000.
(C) Cheque related to Dividend for ₹ 840.
(D) Cheque from Sheela for ₹ 10,500.

Ans :

(D) Cheque from Sheela for ₹ 10,500.
The cash book shows a debit entry 'To Sheela' for ₹ 10,500 on Dec 29th, indicating a cheque was deposited. However, a corresponding credit for this amount does not appear in the December pass book extract. Therefore, this represents a cheque deposited but not yet credited by the bank at the end of the month.

May/June 2012

52. Based on the following extracts for S Trading Company for December 2022: Cash Book shows credit entries 'By George' ₹ 2,000 (Dec 10), 'By White' ₹ 100 (Dec 30), 'By Madanlal' ₹ 4,000 (Dec 30). Bank Pass Book does not show corresponding debits in December. What is the total amount of cheques issued but not presented?
(A) ₹ 9,100
(B) ₹ 6,100
(C) ₹ 2,000
(D) ₹ 4,100

Ans :

(B) ₹ 6,100
The cash book credit side lists cheques issued. Comparing these with the pass book debit side, the cheques issued to George (₹ 2,000), White (₹ 100), and Madanlal (₹ 4,000) do not appear as debits in the pass book. The total of these unpresented cheques is
₹ 2,000 + ₹ 100 + ₹ 4,000 = ₹ 6,100.

Oct/Nov 2014

53. Based on the following extracts for S Trading Company for December 2022: Cash Book extract is provided. Bank Pass Book shows a debit 'To L.I.C. Premium' ₹ 500 (Dec 28). This entry is not in the cash book. Which transaction appears in the pass book but is missing from the cash book, requiring a cash book adjustment?
(A) Payment to Goyal for ₹ 3,000.
(B) Deposit from Geeta for ₹ 5,000.
(C) Payment of L.I.C. Premium of ₹ 500.
(D) Payment to Black for ₹ 5,000.

Ans :

(C) Payment of L.I.C. Premium of ₹ 500.
The pass book shows a debit of ₹ 500 on Dec 28th for 'To L.I.C. Premium'. This payment, likely made under a standing instruction, is not recorded as a credit in the provided cash book extract. Therefore, it is an item that requires a correcting entry to be made in the cash book.

NODIA

May/June 2019

54. The cash book shows a dividend receipt of ₹ 840, while the pass book shows a dividend credit of ₹ 480. How is this difference of ₹ 360 treated when reconciling?
(A) A cheque deposited but not credited.
(B) A direct credit by the bank to be added to the cash book balance.
(C) A cheque issued but not presented.
(D) A clerical error to be subtracted from the cash book balance.

Ans :

(D) A clerical error to be subtracted from the cash book balance.
The reconciliation for this discrepancy assumes the correct dividend was ₹ 480 and the cash book entry of ₹ 840 was an overstatement. Therefore, the excess amount of ₹ 840 - ₹ 480 = ₹ 360 is

subtracted from the cash book balance to correct it.

Oct/Nov 2006

55. Given a starting cash book balance of ₹ 13,740, a clerical error overstating receipts by ₹ 360, and an unrecorded L.I.C. premium payment of ₹ 500, what is the final adjusted (corrected) cashbook balance?
(A) ₹ 12,880
(B) ₹ 13,740
(C) ₹ 8,480
(D) ₹ 14,600

Ans :

(A) ₹ 12,880
Starting with the cash book balance of ₹ 13,740, we must make two adjustments. First, subtract the clerical error related to the dividend (₹ 360). Second, subtract the unrecorded L.I.C. premium payment (₹ 500). The calculation is ₹ 13,740 - ₹ 360 - ₹ 500 = ₹ 12,880, which is the corrected cash book balance.

May/June 2021

56. What is the correct treatment for 'Clerical errors' in the BRS format when starting with the 'Balance as per cashbook'?
(A) Always add them to the balance.
(B) Add or subtract them depending on their net impact on the balance.
(C) Always subtract them from the balance.
(D) Ignore them as they are corrected separately.

Ans :

(B) Add or subtract them depending on their net impact on the balance.
The treatment of clerical errors depends entirely on their nature. An error that understated the balance (e.g., omitting a receipt) would be added. An error that overstated the balance (e.g., posting a payment twice) would be subtracted. Therefore, they are added or subtracted based on their specific impact on the cash book balance.

Oct/Nov 2010

57. Which of the following is NOT a valid reason to prepare a Bank Reconciliation Statement?
(A) To identify delays in cheque clearing and take necessary follow-up action.
(B) To detect potential fraud committed by staff handling cash and cheques.
(C) To determine the correct bank balance at a particular point in time.
(D) To approve a loan application submitted to the bank.

Ans :

(D) To approve a loan application submitted to the bank.
A BRS is an internal control and accounting tool used by a firm to reconcile its records with the bank's records. While a correct financial picture is important for a loan application, the BRS itself is not a tool for approving the loan; that is a function of the bank's credit department based on a holistic assessment.

May/June 2005

58. A scenario involves reconciling balances from a March cash book against an April pass book. Which principle should be applied?
(A) Consider only the common entries that appear in both extracts.
(B) Consider only the uncommon entries from both books.
(C) Consider all entries from the April pass book.
(D) Ignore the March cash book and prepare a new one for April.

Ans :

(A) Consider only the common entries that appear in both extracts.
When reconciling balances where the book periods are different (e.g., March vs. April), the reconciling items are those transactions from the first period (March) that are processed in the second period (April). These are the 'common entries' that bridge the time gap and explain the difference between the March 31st balances.

May/June 2018

59. An April pass book shows debits for Raj & Sons (₹ 800) and Mackmillion Radios (₹ 400). These payments were recorded in the March cash book. As of March 31st, what is the total amount of cheques issued but not yet presented for payment?
(A) ₹ 1,500
(B) ₹ 2,200
(C) ₹ 1,200
(D) ₹ 800

Ans :

(C) ₹ 1,200
We need to find payments recorded in the March cash book that were debited by the bank in April.

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The April pass book shows debits for Raj & Sons (₹ 800) and Mackmillion Radios (₹ 400). These represent cheques issued in March but presented in April. The total is ₹ 800 + ₹ 400 = ₹ 1,200.

Oct/Nov 2016

60. An April pass book shows credits for Dinshaw & Co. (₹ 2,200), Dhanbura & Co. (₹ 5,700), and Anthony (₹ 3,425). These deposits were recorded in the March cash book. What is the total amount of cheques deposited in March but not credited until April?
(A) ₹ 11,325
(B) ₹ 9,375
(C) ₹ 5,700
(D) ₹ 2,200

Ans :

(A) ₹ 11,325
We need to identify deposits from the March cash book that were credited by the bank in April. The April pass book shows credits for Dinshaw & Co. (₹ 2,200), Dhanbura & Co. (₹ 5,700), and Anthony (₹ 3,425). The total of these late-clearing cheques is ₹ 2,200 + ₹ 5,700 + ₹ 3,425 = ₹ 11,325.

May/June 2014

61. Mr. K's pass book for April 1st shows an opening "To Balance (overdraft) ₹ 750". What is the correct starting balance to be used from the bank's records for the BRS as of March 31st?
(A) A credit balance of ₹ 750.
(B) A nil balance.
(C) The closing balance of the March pass book, which is not given.
(D) A debit balance of ₹ 750 (overdraft).

Ans :

(D) A debit balance of ₹ 750 (overdraft).
The opening balance of the April pass book on April 1st represents the closing balance as of the end of the previous day, March 31st. The extract states this is a "To Balance (overdraft) ₹ 750," which is a debit balance from the bank's perspective and should be treated as a negative figure.

Oct/Nov 2007

62. Starting with a pass book overdraft of ₹ 750, cheques deposited but not yet credited of ₹ 11,325, and cheques issued but not yet presented of ₹ 1,200, calculate the adjusted bank balance as of March 31st.
(A) ₹ 11,875
(B) ₹ 9,375
(C) (₹ 2,275)
(D) ₹ 10,875

Ans :

(B) ₹ 9,375
Start with the pass book overdraft (-₹ 750). Add cheques deposited but not yet credited (+₹ 11,325). Subtract cheques issued but not yet presented (-₹ 1,200). The calculation is (-750) + 11,325 - 1,200 = ₹ 9,375. This adjusted balance correctly matches the cash book balance, indicating a successful reconciliation.

May/June 2025

63. Before preparing a Bank Reconciliation Statement, an accountant often adjusts the cash book balance first. Which of the following items would be used for this adjustment?
(A) Cheques issued but not yet presented to the bank.
(B) Cheques deposited but not yet collected by the bank.
(C) Debits for the dishonour of cheques in the pass book.
(D) Errors committed by the bank in the pass book.

Ans :

(C) Debits for the dishonour of cheques in the pass book.
Adjusting the cash book involves recording items that the firm was previously unaware of but which are correctly recorded by the bank. A dishonoured cheque is debited by the bank, and the firm must make a corresponding credit entry in its cash book to correct its balance before preparing the BRS.

Oct/Nov 2019

64. Identify the item that is NOT typically used to adjust the cash book balance before preparing the main BRS.
(A) Direct deposits made by customers of the trader.
(B) Collection of interest on securities by the bank.
(C) Errors committed in the cash book.
(D) Cheques deposited but not yet credited.

Ans :

(D) Cheques deposited but not yet credited.

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'Cheques deposited but not yet credited' is a timing difference. The entry is already correctly recorded in the cash book. It is a reconciling item used in the BRS itself to explain the difference between balances, not an item used to correct or update the cash book balance beforehand.

May/June 2009

65. Which of the following is a primary advantage of preparing a Bank Reconciliation Statement?
(A) It serves as an important internal control technique for management.
(B) It guarantees that the bank will not make any errors in the future.
(C) It automatically corrects all errors in the pass book.
(D) It increases the interest earned on the bank balance.

Ans :

(A) It serves as an important internal control technique for management.
Preparing a BRS is a crucial internal control measure. It provides regular verification of the cash book's accuracy, helps in the timely detection of errors and potential fraud, and gives management a clear picture of the company's actual bank position, thereby enabling better cash management and control over financial resources.

Oct/Nov 2011

66. How does preparing a BRS help in managing cash flow effectively?
(A) It legally obligates customers to pay their dues faster.
(B) It shows the correct, cleared bank balance at any particular time.
(C) It automatically transfers funds between different bank accounts.
(D) It prevents the bank from charging any service fees.

Ans :

(B) It shows the correct, cleared bank balance at any particular time.
A key benefit of reconciliation is that it reveals the true, spendable balance available in the bank after accounting for unpresented cheques and uncleared deposits. Knowing this correct balance is vital for effective cash flow management, as it helps prevent the issuance of cheques that might bounce due to insufficient cleared funds.

Oct/Nov 2024

67. The process of preparing a BRS can help reveal frauds committed by staff. Which of the following scenarios is an example of this?
(A) A bank teller incorrectly entering a deposit amount.
(B) The bank charging a higher-than-agreed interest rate on an overdraft.
(C) A cheque being delayed in the clearing house.
(D) An employee depositing a customer's cheque but not recording it in the cash book.

Ans :

(D) An employee depositing a customer's cheque but not recording it in the cash book.
If a staff member suppresses the recording of a receipt in the cash book (a form of 'teeming and lading' or misappropriation), the pass book will show a higher balance. The regular process of reconciliation would highlight this discrepancy (a credit in the pass book with no corresponding debit in the cash book), revealing the irregularity.

May/June 2017

68. What is meant by a 'Favourable Balance' in the context of a BRS?
(A) A positive balance in the bank account, shown as a debit in the cash book.
(B) A debit balance as per the pass book.
(C) A credit balance as per the cash book.
(D) The total amount of unpresented cheques.

Ans :

(A) A positive balance in the bank account, shown as a debit in the cash book.
A 'Favourable Balance' means the firm has funds in its account; it is an asset. This is represented by a debit balance in the bank column of the cash book. In the pass book, this same favourable balance would be shown as a credit balance, as it is a liability of the bank to the firm.

Oct/Nov 2005

69. A 'Standing Instruction' is a key term related to BRS. What does it signify?
(A) An instruction from the bank to the customer to maintain a minimum balance.
(B) A legal notice served for a dishonoured cheque.
(C) An authorization given by the customer to the bank to make regular, periodic payments.
(D) A daily report of all transactions sent by the bank.

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Ans :

(C) An authorization given by the customer to the bank to make regular, periodic payments.
A standing instruction is a pre-authorization given by an account holder to their bank to perform specific transactions on their behalf. This often includes making recurring payments like insurance premiums or loan installments, or collecting recurring receipts like dividends, without requiring separate instructions for each transaction.

May/June 2020

70. Which of the following statements is INCORRECT regarding the features of a Bank Reconciliation Statement (BRS)?
(A) A BRS is prepared by the bank and sent to the customer.
(B) A BRS helps in arriving at the actual cleared position of the bank balance.
(C) A BRS identifies and records delays in the clearing of cheques.
(D) A BRS is a tool that can help in the detection of fraud related to cheques.

Ans :

(A) A BRS is prepared by the bank and sent to the customer.
The Bank Reconciliation Statement is an internal statement prepared by the firm or account holder, not by the bank. The bank provides the passbook or bank statement, which is one of the source documents. The firm's accountant then uses this to reconcile it with their own cash book records.

May/June 2013

71. A bank statement is essentially a copy of which of the following?
(A) The customer's account as maintained in the bank's ledger.
(B) The cash column of the customer's cash book.
(C) The bank column of the bank's own cash book.
(D) The petty cash book of the customer.

Ans :

(A) The customer's account as maintained in the bank's ledger.
A bank statement or passbook is the bank's record of the customer's transactions. It is a direct copy or extract of the customer's account from the bank's own books of accounts (its ledger). It reflects the bank's perspective of the financial relationship and all transactions processed through the account during a period.

Oct/Nov 2021

72. If the receipts side of a cash book is overcast by ₹ 1,000, what is the effect on the cash book balance and how is it rectified in a BRS?
(A) The balance is overstated; ₹ 1,000 is added during reconciliation.
(B) The balance is overstated; ₹ 1,000 is subtracted during reconciliation.
(C) The balance is understated; ₹ 1,000 is added during reconciliation.
(D) The balance is understated; ₹ 1,000 is subtracted during reconciliation.

Ans :

(B) The balance is overstated; ₹ 1,000 is subtracted during reconciliation.
Overcasting the receipts side means the total receipts are shown as higher than they actually are. This inflates the cash book balance, making it overstated by ₹ 1,000. To correct this and arrive at the true balance, this excess amount of ₹ 1,000 must be subtracted from the cash book balance during reconciliation.

May/June 2024

73. A credit balance of ₹ 5,000 in the cash book was mistakenly carried forward as a debit balance of ₹ 5,000 on the next page. How will this error be reconciled?
(A) By crediting ₹ 5,000 in the adjusted cash book.
(B) By debiting ₹ 5,000 in the adjusted cash book.
(C) By crediting ₹ 10,000 in the adjusted cash book.
(D) By debiting ₹ 10,000 in the adjusted cash book.

Ans :

(C) By crediting ₹ 10,000 in the adjusted cash book.
The original balance should have been a credit of ₹ 5,000 (-5,000). It was wrongly posted as a debit of ₹ 5,000 (+5,000). The error is the difference between the wrong posting and the correct posting: +5,000 - (-5,000) = +10,000. To nullify this overstatement of ₹ 10,000, a credit of ₹ 10,000 is required in the adjusted cash book.

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Oct/Nov 2008

74. In a situation with no overdraft facility, a direct deposit by a customer into the firm's bank account will result in which of the following states before reconciliation?

(A) The cash book balance will be higher than the passbook balance.
(B) Both balances will be equal but incorrect.
(C) The passbook balance will be lower than the cash book balance.
(D) The passbook balance will be higher than the cash book balance.

Ans :

(D) The passbook balance will be higher than the cash book balance.
The bank immediately credits the account upon the direct deposit, increasing the passbook balance. The firm, being unaware of the transaction until it sees the statement, has not yet made a corresponding debit entry in its cash book. Consequently, the passbook balance will be higher than the cash book balance.

May/June 2006

75. Identify the correct pair of a BRS item and its treatment when starting the reconciliation from the Balance as per Pass Book.

(A) Cheques issued but not presented : Subtracted
(B) Cheques issued but not presented : Added
(C) Bank charges not in cash book : Subtracted
(D) Cheques deposited but not credited : Subtracted

Ans :

(A) Cheques issued but not presented : Subtracted
When starting with the pass book balance, we adjust for items already in the cash book but not yet in the pass book. Cheques issued have reduced the cash book balance. Since they are not yet paid by the bank, the pass book balance is higher. To reconcile, we must subtract this amount from the pass book balance.

Oct/Nov 2017

76. Which of the following statements about the relationship between a cash book and a pass book is correct?

(A) A credit balance in the cash book corresponds to a credit balance in the pass book.
(B) A credit balance in the cash book represents an overdraft for the firm.
(C) A debit entry in the cash book for a deposit corresponds to a debit entry in the pass book.
(D) The pass book is prepared by the company's accountant as a copy of the cash book.

Ans :

(B) A credit balance in the cash book represents an overdraft for the firm.
In the bank column of a cash book, a debit balance signifies cash at bank (an asset). Conversely, a credit balance signifies that the firm has withdrawn more than it has, representing an overdraft (a liability). This is the correct interpretation among the given options, as the others describe the relationships incorrectly.

May/June 2008

77. Which of the following is an example of a timing difference and not an error?

(A) Recording a cheque of ₹ 980 as ₹ 890 in the cash book.
(B) Forgetting to record a cash deposit in the cash book.
(C) A bank debiting charges to the wrong customer account.
(D) A cheque issued to a creditor in late March, which is paid by the bank in early April.

Ans :

(D) A cheque issued to a creditor in late March, which is paid by the bank in early April.
A timing difference arises from the lag between when a transaction is recorded in the cash book and when it is processed by the bank. A cheque issued in one month and cleared in the next is a perfect example. The other options describe clear errors made by either the firm or the bank.

Oct/Nov 2013

78. In the process of adjusting the cash book before preparing the BRS, which of the following would be recorded as a credit entry?

(A) Interest on overdraft charged by the bank.
(B) Dividend collected by the bank.
(C) Direct deposit by a customer.
(D) Interest credited by the bank on a positive balance.

Ans :

(A) Interest on overdraft charged by the bank.
Interest on overdraft is an expense for the firm. When the bank debits the pass book for this charge, the firm must make a corresponding entry in its cash book. Since it is an expense

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that reduces the bank balance (or increases the overdraft), it is recorded as a credit entry in the cash book's bank column.

May/June 2015

79. Match List-I with List-II regarding their treatment in a Bank Reconciliation Statement starting from the cash book balance.

List-I (Item)

P. Cheque issued but not presented
Q. Bank charges
R. Cheque deposited but not cleared
S. Dividend collected by bank

List-II (Treatment)

1. Add to cash book balance
2. Subtract from cash book balance
3. No treatment in cash book

(A) P-3, Q-2, R-3, S-1
(B) P-1, Q-2, R-2, S-1
(C) P-3, Q-1, R-3, S-2
(D) P-2, Q-2, R-1, S-1

Ans :

(A) P-3, Q-2, R-3, S-1
When starting from the cash book balance to find the adjusted cash book balance, P (Cheque issued but not presented) and R (Cheque deposited but not cleared) are timing differences and are not used to adjust the cash book itself (No treatment). Q (Bank charges) is an unrecorded expense and must be subtracted. S (Dividend collected) is unrecorded income and must be added.

Oct/Nov 2012

80. A firm's cash book showed a bank balance of ₹ 25,000. It was discovered that a cheque issued for ₹ 2,000 was not presented and a cheque deposited for ₹ 3,000 was not cleared. Also, the bank had credited ₹ 500 as interest. What is the balance as per pass book?

(A) ₹ 23,500
(B) ₹ 24,500
(C) ₹ 25,500
(D) ₹ 26,500

Ans :

(A) ₹ 23,500
To find the pass book balance from the cash book balance, adjust for all reconciling items. Start with the cash book balance of ₹ 25,000. Add cheques issued but not presented (₹ 2,000). Subtract cheques deposited but not cleared (₹ 3,000). Subtract interest credited by the bank but not yet in the cash book (₹ 500). The calculation is ₹ 25,000 + ₹ 2,000 - ₹ 3,000 - ₹ 500 = ₹ 23,500.

May/June 2011

81. Consider the following statements:

1. A bank reconciliation statement is part of the double-entry system.
2. A bank reconciliation statement is prepared to find out the causes of differences between the cash book and pass book balances.

Which of the above statements is/are correct?

(A) Only 1
(B) Only 2
(C) Both 1 and 2
(D) Neither 1 nor 2

Ans :

(B) Only 2
A Bank Reconciliation Statement is a memorandum statement, not a formal part of the double-entry accounting system like a ledger or journal. Its primary purpose is to identify and explain the discrepancies between the bank balance as per the company's cash book and the balance as per the bank's statement, making statement 2 correct and statement 1 incorrect.

Oct/Nov 2020

82. What is the correct accounting principle applied to the bank column in a firm's cash book?

(A) Debit what comes in, and Credit what goes out.
(B) Debit the receiver, and Credit the giver.
(C) Debit all expenses and losses, and Credit all incomes and gains.
(D) Debit the giver, and Credit the receiver.

Ans :

(B) Debit the receiver, and Credit the giver.
The bank account is treated as a personal account in the firm's books. When money is deposited, the bank is the receiver, so its account is debited. When a payment is made through the bank, the bank is the giver on behalf of the firm, so its account is credited. This follows the rule for personal accounts.

May/June 2022

83. A debit entry in the pass book corresponds to which of the following in the cash book?

(A) A debit entry, representing a deposit.
(B) A contra entry.
(C) A credit entry, representing a payment or

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withdrawal.
(D) No entry is made in the cash book.

Ans :

(C) A credit entry, representing a payment or withdrawal.
A debit entry in the pass book signifies a reduction in the customer's account balance from the bank's perspective (e.g., a cheque payment or bank charge). This corresponds to a payment or withdrawal from the firm's point of view, which is recorded as a credit entry in the bank column of the firm's cash book.

Oct/Nov 2023

84. Which of the following causes for the difference between cash book and pass book balances will be self-correcting over time?
(A) An error of casting in the cash book.
(B) Omission of a bank charge entry in the cash book.
(C) An incorrect amount debited by the bank.
(D) Cheques deposited but not yet collected.

Ans :

(D) Cheques deposited but not yet collected.
'Cheques deposited but not yet collected' is a timing difference. The discrepancy it causes is temporary. Once the cheque clears through the banking system, the bank will credit the account, and this particular reconciling item will automatically resolve itself without any corrective journal entry being needed in the cash book, as the initial entry was correct.

Oct/Nov 2015

85. **Assertion (A) :** The adjusted cash book balance should be equal to the adjusted bank balance for a successful reconciliation.
Reason (R) : The adjusted cash book balance is a notional figure, while the adjusted bank balance is the actual balance that goes to the balance sheet.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(C) (A) is true but (R) is false.
Assertion (A) is the fundamental principle of BRS completion. However, Reason (R) is false. The 'adjusted bank balance' is the notional figure used for comparison, whereas the 'adjusted (corrected) cash book balance' is the actual, true balance that is subsequently reported in the trial balance and the balance sheet after all omissions and errors are accounted for.

May/June 2010

86. Which of the following statements is INCORRECT?
(A) A debit balance in the cash book is a favourable balance.
(B) A debit balance in the pass book is a favourable balance.
(C) A credit balance in the pass book is a favourable balance.
(D) A credit balance in the cash book is an overdraft.

Ans :

(B) A debit balance in the pass book is a favourable balance.
A debit balance in the pass book (or bank statement) indicates that the bank has debited the customer's account more than it has credited it. This means the customer has a negative balance, or an overdraft, which is an unfavourable balance. All other statements correctly describe the nature of the balances from their respective viewpoints.

Oct/Nov 2022

87. Consider the following three types of reconciling items:
1. Cheques issued but not presented.
2. Interest on overdraft charged by the bank.
3. Cheques deposited but not collected.

Which of these do NOT require a change in the cash book?
(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(C) 1 and 3 only
Items 1 and 3 are timing differences. The entries for issuing and depositing cheques are already correctly recorded in the cash book. They are merely waiting to be processed by the bank. Item 2, interest on overdraft, is an entry made by the

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bank that the company needs to record, thus requiring a change in the cash book.

May/June 2016

88. A company's bank statement shows a credit balance of ₹ 50,000. The cash book has a debit balance of ₹ 46,000. The only reconciling items are unpresented cheques of ₹ 7,000 and uncredited deposits. What is the amount of the uncredited deposits?
(A) ₹ 3,000
(B) ₹ 11,000
(C) ₹ 4,000
(D) ₹ 1,000

Ans :

(A) ₹ 3,000
The reconciliation equation is: Balance as per Pass Book + Uncredited Deposits - Unpresented Cheques = Balance as per Cash Book. Let the uncredited deposits be X. So, ₹ 50,000 + X - ₹ 7,000 = ₹ 46,000. This simplifies to ₹ 43,000 + X = ₹ 46,000. Therefore, X = ₹ 46,000 - ₹ 43,000 = ₹ 3,000.

Oct/Nov 2009

89. On 31st March, the cash book showed a bank overdraft of ₹ 10,000. Cheques issued but not presented amounted to ₹ 3,000. Cheques deposited but not cleared amounted to ₹ 4,000. The bank had wrongly debited the account with ₹ 500. What is the balance as per the bank statement?
(A) Overdraft of ₹ 9,500
(B) Favourable balance of ₹ 11,500
(C) Overdraft of ₹ 11,500
(D) Favourable balance of ₹ 9,500

Ans :

(C) Overdraft of ₹ 11,500
To find the bank statement balance, we reconcile to the true balance. The adjusted cash book balance is -₹10,000 (as there are no items to adjust in it). The adjusted bank balance must also equal this. Let the bank balance be X. The formula is:
X + (uncleared deposits) - (unpresented cheques) + (wrongful debits) = Adjusted Balance.
So,
X + ₹ 4,000 - ₹ 3,000 + ₹ 500 = -₹ 10,000.
This simplifies to X + ₹ 1,500 = -₹ 10,000, so X = -₹ 11,500.

May/June 2023

90. Identify the incorrect pair.
(A) Overdraft as per cash book : Debit Balance
(B) Overdraft as per pass book : Debit Balance
(C) Favourable balance as per cash book : Debit Balance
(D) Favourable balance as per pass book : Credit Balance

Ans :

(A) Overdraft as per cash book : Debit Balance
An overdraft as per the cash book signifies a liability for the firm, meaning it has paid out more from its bank account than it has deposited. In the cash book's bank column, liabilities are represented by a credit balance. A debit balance would indicate a favourable balance (asset).

Oct/Nov 2018

91. The main purpose of adjusting the cash book before preparing the BRS is to:
(A) Record all timing differences.
(B) Correct the errors made by the bank in the pass book.
(C) Calculate a notional balance for comparison purposes only.
(D) Ensure the cash book reflects the true balance by including all transactions already processed by the bank.

Ans :

(D) Ensure the cash book reflects the true balance by including all transactions already processed by the bank.
The pre-BRS adjustment of the cash book is done to update it with items the company was unaware of, like bank charges, direct deposits, or interest. This brings the cash book balance to its true, corrected state, reflecting all transactions that have actually occurred and been processed by the bank, before reconciling it with the passbook for timing differences.

May/June 2007

92. A cheque for ₹ 5,000 was deposited into the bank but was dishonoured. The bank debited the account. How should this be treated to reconcile the books?
(A) It should be added to the pass book balance in the BRS.
(B) It should be recorded on the credit side of the cash book.
(C) It should be subtracted from the pass book

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balance in the BRS.
(D) It is a timing difference and requires no entry.

Ans :

(B) It should be recorded on the credit side of the cash book.
When the cheque was deposited, the cash book was debited. Its dishonour means the funds were not received. The bank corrects this by debiting the pass book. To reflect this reality, the firm must reverse its original entry by crediting the bank column of the cash book, thereby reducing its recorded bank balance.

Oct/Nov 2025

93. Which of the following four statements are correct?
1. The BRS is prepared at the end of the financial year only.
2. A BRS helps in detecting errors in the cash book and the pass book.
3. A debit balance in the pass book means an overdraft.
4. Cheques deposited but not credited are subtracted from the pass book balance in a BRS.

(A) 1 and 4
(B) 2 and 3
(C) 1, 2, and 3
(D) 2, 3, and 4

Ans :

(B) 2 and 3
Statement 2 is correct, as BRS is a tool for error detection. Statement 3 is also correct; a debit balance in the pass book is an overdraft. Statement 1 is incorrect; BRS is usually prepared monthly or at more regular intervals. Statement 4 is incorrect; cheques deposited but not credited are added to the pass book balance.

May/June 2012

94. A payment of ₹ 1,250 was recorded twice in the pass book by the bank. The cash book is correct. The pass book shows an overdraft of ₹ 8,000. What is the correct overdraft?
(A) ₹ 9,250
(B) ₹ 10,500
(C) ₹ 5,500
(D) ₹ 6,750

Ans :

(D) ₹ 6,750
The pass book shows an overdraft of ₹ 8,000. A payment was recorded twice, meaning the account was debited an extra ₹ 1,250. This wrongful debit increased the overdraft shown. The correct overdraft is therefore ₹ 8,000 - ₹ 1,250 = ₹ 6,750. The bank balance should have been higher (or overdraft lower) by the amount of the error.

Oct/Nov 2014

95. Choose the most appropriate statement.
(A) A Bank Reconciliation Statement is prepared to know the reasons for disagreement between two balances.
(B) A Bank Reconciliation Statement is a part of the final accounts.
(C) A Bank Reconciliation Statement is prepared only when there is an overdraft.
(D) A Bank Reconciliation Statement is prepared by the auditors of the company.

Ans :

(A) A Bank Reconciliation Statement is prepared to know the reasons for disagreement between two balances.
This statement captures the core purpose of a BRS most accurately. It is a diagnostic tool created specifically to identify, list, and understand the reasons (timing differences, errors, omissions) for the discrepancy between the cash book's bank balance and the pass book's balance, facilitating control and accuracy in financial reporting.

May/June 2019

96. A cheque of ₹ 450 was recorded in the cash column of the cash book instead of the bank column. How is this error rectified during cash book adjustment?
(A) By debiting the bank column with ₹ 450.
(B) By debiting the bank column and crediting the cash column with ₹ 450.
(C) By crediting the bank column with ₹ 450.
(D) By debiting the cash column and crediting the bank column with ₹ 450.

Ans :

(B) By debiting the bank column and crediting the cash column with ₹ 450.
The error was that a bank transaction was treated as a cash transaction. To correct this within the cash book, the bank column must be debited (as it was a deposit) and the cash column must be credited to reverse the incorrect entry. This is a

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contra-style correction to move the amount to the correct column.

Oct/Nov 2006

97. The payments side of the cash book was undercast by ₹ 200. This is an error that will:
(A) Decrease the cash book balance by ₹ 200.
(B) Increase the pass book balance by ₹ 200.
(C) Decrease the pass book balance by ₹ 200.
(D) Increase the cash book balance by ₹ 200.

Ans :

(D) Increase the cash book balance by ₹ 200.
Undercasting the payments (credit) side means the total deductions from the balance are understated. If payments are shown as ₹ 200 less than they actually were, the resulting cash book balance will be artificially inflated or higher by ₹ 200. To correct this, ₹ 200 must be subtracted from the cash book balance.

May/June 2021

98. Consider the following statements:
Statement I : A Bank Reconciliation Statement is prepared with the balance of either the cash book or the pass book as a starting point.
Statement II : The object of preparing a BRS is to bring the cash book balance in agreement with the pass book balance.
(A) Both Statement I and Statement II are true.
(B) Both Statement I and Statement II are false.
(C) Statement I is true, but Statement II is false.
(D) Statement I is false, but Statement II is true.

Ans :

(A) Both Statement I and Statement II are true.
Statement I is true; the reconciliation process can start with either balance. Statement II is also true; the ultimate objective is to account for all differences so that the adjusted balances agree, thereby confirming the accuracy of both sets of records after accounting for timing differences and correcting errors or omissions.

Oct/Nov 2010

99. Match List-I (Transaction) with List-II (First Appearance).
List-I
P. Direct deposit by a customer
Q. Cheque issued to a supplier
R. Life insurance premium paid under SI
S. Cheque deposited by the company
List-II
1. Credit side of Cash Book
2. Debit side of Cash Book
3. Credit side of Pass Book
4. Debit side of Pass Book
(A) P-3, Q-1, R-4, S-2
(B) P-4, Q-2, R-3, S-1
(C) P-3, Q-2, R-4, S-1
(D) P-4, Q-1, R-3, S-2

Ans :

(A) P-3, Q-1, R-4, S-2
P (Direct deposit) first appears as a credit in the pass book. Q (Cheque issued) is first recorded on the credit side of the cash book. R (Premium paid under SI) is first debited by the bank in the pass book. S (Cheque deposited) is first recorded on the debit side of the cash book.

May/June 2005

100. If the starting point of a BRS is the overdraft as per the cash book, how would 'interest on overdraft' charged by the bank (not yet recorded in cash book) be treated?
(A) It would be added to the overdraft balance.
(B) It would be subtracted from the overdraft balance.
(C) It would be ignored.
(D) It would be shown as a separate statement.

Ans :

(A) It would be added to the overdraft balance.
The starting point is overdraft as per cash book (a credit/negative balance). Interest on overdraft is an additional expense that increases the amount owed to the bank. Therefore, this unrecorded charge must be added to the existing overdraft balance, making the total overdraft larger. This is equivalent to crediting the cash book.

May/June 2018

101. Which of the following five statements regarding BRS are correct?
1. It is a memorandum statement.
2. It helps in detecting frauds and errors.
3. It must be prepared only on 31st March.
4. It is prepared by the bank.
5. It reconciles the bank column of the cash book with the bank statement.
(A) 1, 2, 3
(B) 2, 3, 5
(C) 1, 2, 5
(D) 1, 4, 5

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Ans :

(C) 1, 2, 5
Statement 1 is correct (it's a memorandum statement). Statement 2 is correct (it's a control tool). Statement 5 is correct (it reconciles the specified accounts). Statement 3 is incorrect (it's prepared regularly, often monthly). Statement 4 is incorrect (it's prepared by the account holder/ firm). Therefore, statements 1, 2, and 5 are correct.

Oct/Nov 2016

102. A debit balance of ₹ 1,526 was brought forward as a credit balance of ₹ 1,526. What is the value and nature of the error?
(A) ₹ 1,526 debit error.
(B) ₹ 3,052 debit error.
(C) ₹ 1,526 credit error.
(D) ₹ 3,052 credit error.

Ans :

(B) ₹ 3,052 debit error.
The correct opening balance was a debit of ₹ 1,526. By posting it as a credit, the balance was reduced by ₹ 1,526 from what it should have been, and then further reduced by another ₹ 1,526. The total understatement is ₹ 1,526 + ₹ 1,526 = ₹ 3,052. To fix this, a debit entry of ₹ 3,052 is required, which can be termed a debit error correction.

May/June 2014

103. The closing balance in the Bank Statement is ₹ 15,534. Cheques deposited but not yet credited are nil. Cheques issued but not presented are ₹ 3,699. What is the adjusted balance in the bank statement?
(A) ₹ 19,233
(B) ₹ 15,534
(C) ₹ 11,835
(D) ₹ 12,835

Ans :

(C) ₹ 11,835
The calculation for the adjusted bank statement balance starts with the closing balance as per the bank statement. To this, we add cheques deposited but not yet credited and subtract cheques issued but not presented. The calculation is: ₹ 15,534 + ₹ 0 - ₹ 3,699 = ₹ 11,835. This is the notional reconciled balance.

Oct/Nov 2007

104. A firm's overdraft as per pass book is ₹ 12,000. Cheques deposited but not yet credited amount to ₹ 3,000. Cheques issued but not presented amount to ₹ 4,000. What is the adjusted bank balance?
(A) Overdraft of ₹ 11,000
(B) Favourable balance of ₹ 1,000
(C) Overdraft of ₹ 5,000
(D) Overdraft of ₹ 13,000

Ans :

(D) Overdraft of ₹ 13,000
Starting with an overdraft balance means we begin with a negative figure. The calculation is: (-₹ 12,000) + (cheques deposited but not credited ₹ 3,000) - (cheques issued but not presented ₹ 4,000) . This equals -12,000 + 3,000 - 4,000 = -₹ 13,000, which represents an overdraft of ₹ 13,000.

May/June 2025

105. A cash book shows a credit balance of ₹ 12,300. Credit entries not in cash book are ₹ 1,000, and debit entries not in cash book are ₹ 1,700. What is the adjusted cash book balance?
(A) Credit balance of ₹ 13,000
(B) Credit balance of ₹ 11,600
(C) Debit balance of ₹ 13,000
(D) Credit balance of ₹ 14,000

Ans :

(A) Credit balance of ₹ 13,000
A credit balance in the cash book represents an overdraft, so we start with (-₹ 12,300). Credit entries not in the cash book (like direct deposits) are receipts, which reduce the overdraft, so they are added (+₹ 1,000). Debit entries not in the cash book (like bank charges) are payments, which increase the overdraft, so they are subtracted (-₹ 1,700). The calculation is (-12,300) + 1,000 - 1,700 = -₹ 13,000, a credit balance of ₹ 13,000.

Oct/Nov 2019

106. When comparing cash book and pass book extracts for different, consecutive periods (e.g., Cash book for March, Pass book for April), what do the 'common entries' represent?
(A) Errors made in both periods.
(B) Timing differences that existed at the end of the first period.
(C) Transactions that were correctly recorded and cleared in the first period.
(D) Transactions that occurred only in the second

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period.

Ans :

(B) Timing differences that existed at the end of the first period.
Common entries are those recorded in the cash book in the first period (March) but only processed by the bank in the second period (April). These are precisely the unpresented cheques and uncleared deposits that constituted the timing differences and were the reconciling items as of the end of the first period (March 31st).

May/June 2009

107. From a cash book extract for S Trading Company, credit entries for Dec 30th are: 'By White' for ₹ 100 and 'By Madanlal' for ₹ 4,000. What is the total amount of cheques issued on Dec 30th?
(A) ₹ 100
(B) ₹ 4,000
(C) ₹ 840
(D) ₹ 4,100

Ans :

(D) ₹ 4,100
Looking at the credit side of the cash book extract for S Trading Company, there are two entries for cheques issued on December 30th. These are 'By White' for ₹ 100 and 'By Madanlal' for ₹ 4,000. The total amount of cheques issued on that specific date is the sum of these two, which is ₹ 100 + ₹ 4,000 = ₹ 4,100.

Oct/Nov 2011

108. An extract from a pass book for April shows the entry 'To Raj & Sons - Debit ₹ 800' on Apr 2. For a BRS being prepared for March 31st, what does this entry represent?
(A) A cheque issued in March but not presented for payment until April.
(B) A cheque deposited but not yet credited.
(C) A bank charge for the month of April.
(D) A direct payment made by Mr. K in April.

Ans :

(A) A cheque issued in March but not presented for payment until April.
This debit in the April pass book signifies a payment made by the bank. Since it is being used to reconcile the March 31st balance, it represents a cheque that Mr. K had issued and recorded in his March cash book, but the payee only presented it for payment in April, making it an unpresented cheque.

Oct/Nov 2024

109. An extract from a pass book for April shows the entry 'By Dhanbura & Co. - Credit ₹ 5,700' on Apr 3. How is this treated in the March 31st BRS?
(A) A cheque issued but not presented.
(B) A direct deposit by a customer in April.
(C) A cheque deposited but not yet credited.
(D) An error by the bank.

Ans :

(C) A cheque deposited but not yet credited.
This credit entry in the April pass book indicates a deposit has been cleared and credited. As it's a common entry with the March cash book for the March 31st BRS, it signifies a cheque that Mr. K deposited in March, but it only cleared and was credited to his account by the bank in April.

May/June 2017

110. Based on a pass book extract for April showing credits 'By Dinshaw & Co.' (₹ 2,200), 'By Dhanbura & Co.' (₹ 5,700), and 'By Anthony' (₹ 3,425), what is the total amount for 'Cheques deposited but not yet credited' in the March 31st BRS?
(A) ₹ 11,325
(B) ₹ 7,900
(C) ₹ 5,700
(D) ₹ 2,200

Ans :

(A) ₹ 11,325
The items representing cheques deposited in March but credited in April are 'By Dinshaw & Co.' (₹ 2,200), 'By Dhanbura & Co.' (₹ 5,700), and 'By Anthony' (₹ 3,425). The total for this category is the sum of these amounts: ₹ 2,200 + ₹ 5,700 + ₹ 3,425 = ₹ 11,325.

Oct/Nov 2005

111. The final BRS for Mr. K as of 31st March 2022 shows 'Nil' for 'Adjustments made to cashbook'. What does this imply?
(A) Mr. K's cash book contained numerous errors that cancelled each other out.
(B) There were no bank charges, direct deposits, or other such items in the April pass book.
(C) The bank did not process any transactions in April.
(D) All differences between the cash book and pass book were purely due to timing

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differences.

Ans :

(D) All differences between the cash book and pass book were purely due to timing differences. 'Adjustments made to cashbook' are for items like unrecorded bank charges, interest, or direct deposits. Since this section is 'Nil', it means no such items requiring cash book correction were identified for the March 31st reconciliation. All discrepancies were explained by timing differences (unpresented and uncleared cheques) alone.

May/June 2020

112. One of the advantages of a BRS is that it "reveals frauds committed by the staff handling cash and cheques". Which of the following would a BRS most likely reveal?

(A) An employee forging the signature on a company cheque.
(B) An employee withholding a cheque received from a customer instead of depositing it.
(C) An employee stealing physical cash from the office safe.
(D) An employee overstating travel expenses on a reimbursement form.

Ans :

(B) An employee withholding a cheque received from a customer instead of depositing it.
If an employee receives a cheque from a customer and records it in the cash book but does not deposit it into the bank (intending to misappropriate it later), the BRS will show this as a 'cheque deposited but not credited'. If this item remains outstanding for an unusually long time, it prompts an investigation, revealing the fraud.

May/June 2013

113. Arrange the following steps for preparing a BRS in the correct sequence, assuming an adjusted cash book is prepared first.

1. Prepare the Bank Reconciliation Statement.
2. Compare the cash book and pass book to identify differences.
3. Update the cash book with omissions and errors.
4. Arrive at the adjusted cash book balance.

(A) 2, 1, 3, 4
(B) 1, 2, 3, 4
(C) 2, 3, 4, 1
(D) 3, 4, 2, 1

Ans :

(C) 2, 3, 4, 1
The logical process begins with comparing the two documents to find discrepancies (2). Next, the cash book is corrected for items like bank charges and internal errors (3). This leads to the new, adjusted cash book balance (4). Finally, the BRS is prepared using this adjusted balance to reconcile with the pass book balance based on timing differences (1).

Oct/Nov 2021

114. Which of the following is NOT a cause for difference between passbook and cashbook balances?

(A) Errors in casting.
(B) Cheques issued but not presented.
(C) Dishonour of a cheque.
(D) Contra entries.

Ans :

(D) Contra entries.
A contra entry, such as depositing cash into the bank or withdrawing cash for office use, affects both the cash and bank columns of the cash book simultaneously. While it is a transaction, it does not inherently cause a discrepancy between the cash book's bank column and the pass book, unlike the other options which are errors or timing differences.

May/June 2024

115. A bank credits ₹ 5,000 to a firm's account for interest. This will lead to:

(A) An increase in the pass book balance.
(B) An increase in the cash book balance.
(C) A decrease in the pass book balance.
(D) A decrease in the cash book balance.

Ans :

(A) An increase in the pass book balance.
When the bank credits the account for interest, it increases the funds in the account from the bank's perspective, thus increasing the pass book balance. The firm's cash book balance will only increase after the firm becomes aware of this credit and makes a corresponding debit entry. Initially, only the pass book balance changes.

Oct/Nov 2008

116. A company's accountant made the following errors:

1. A cheque issued for ₹ 780 was recorded as ₹

870.
2. A deposit of ₹ 500 was omitted from the cash book.

What is the net effect of these errors on the cash book balance?
(A) Overstated by ₹ 410.
(B) Understated by ₹ 590.
(C) Understated by ₹ 410.
(D) Overstated by ₹ 590.

Ans :

(B) Understated by ₹ 590.
Error 1: A payment of ₹ 780 was recorded as ₹ 870. This overstates the payment side by ₹ 90, which understates the closing balance by ₹ 90. Error 2: A deposit of ₹ 500 was omitted. This understates the receipt side by ₹ 500, which understates the closing balance by ₹ 500. The combined effect is an understatement of ₹ 90 + ₹ 500 = ₹ 590.

May/June 2006

117. An 'overdrawn balance' is also known as:
(A) A favourable balance.
(B) A positive balance.
(C) A credit balance as per pass book.
(D) An unfavourable balance.

Ans :

(D) An unfavourable balance.
An overdrawn balance, or overdraft, signifies that the account holder has withdrawn more money than was available in the account, creating a liability to the bank. This situation is considered unfavourable from the account holder's perspective, as it represents debt rather than an asset. It is a debit balance in the pass book.

Oct/Nov 2017

118. Which of the following transactions will appear on the debit side of a pass book?
(A) Amount paid by the bank as per standing instruction.
(B) Cash deposited into the bank.
(C) Dividend collected by the bank on behalf of the customer.
(D) Interest allowed by the bank on the customer's balance.

Ans :

(A) Amount paid by the bank as per standing instruction.
The debit side of the pass book reflects all outflows or reductions from the account balance. A payment made by the bank based on a standing instruction, such as an insurance premium, is a withdrawal from the customer's account. Therefore, the bank will debit the account to record this transaction.

May/June 2008

119. A BRS is prepared on a monthly basis. A cheque deposited on March 30th is credited by the bank on April 2nd. In which BRS will this appear as a reconciling item?
(A) The BRS for April.
(B) Both the BRS for March and April.
(C) The BRS for March.
(D) Neither, as it clears within a few days.

Ans :

(C) The BRS for March.
As of March 31st, the cheque has been recorded in the cash book but not yet credited in the pass book. This creates a discrepancy that must be explained in the March BRS as a 'cheque deposited but not yet credited'. By the time the April BRS is prepared, the item will have cleared and will no longer be a reconciling item.

Oct/Nov 2013

120. Identify the correct statement regarding the preparation of a BRS.
(A) It is an important control technique for management over cash and bank transactions.
(B) It is mandatory for all businesses under the Companies Act.
(C) It can only be prepared if the cash book shows a debit balance.
(D) It is a statement that reconciles the cash column of the cash book with the pass book.

Ans :

(A) It is an important control technique for management over cash and bank transactions.
While not legally mandatory for all entities, preparing a BRS is a fundamental aspect of good financial governance. It serves as a vital internal control mechanism, allowing management to verify accounting accuracy, monitor cash flows, and detect irregularities or potential fraud in a timely manner, ensuring effective control over bank transactions.

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May/June 2015

121. The balance in an operating account is treated like cash available with the firm because:
(A) It is insured by the government.
(B) It is always shown as a debit balance.
(C) It can be withdrawn whenever desired.
(D) It does not fluctuate.

Ans :

(C) It can be withdrawn whenever desired.
The key characteristic that makes a bank operating account equivalent to cash is its liquidity. The funds are available on demand for the firm to use for payments and other operational needs. This immediate accessibility is why it is considered part of the firm's readily available cash resources for financial management purposes.

Oct/Nov 2012

122. If a firm's passbook shows a credit balance, from the bank's perspective, the firm is a:
(A) Debtor
(B) Creditor
(C) Partner
(D) Agent

Ans :

(B) Creditor
When a firm deposits money, the bank owes that money back to the firm. In this relationship, the firm has given a resource (money) to the bank, making the firm a creditor. The bank's liability to the firm is reflected as a credit balance in the firm's account in the bank's own ledger (the passbook).

May/June 2011

123. A business receives a cheque, and the accountant immediately records it on the debit side of the cash book. This entry signifies:
(A) A decrease in the firm's bank balance.
(B) A payment made by the firm.
(C) An increase in the firm's recorded bank balance.
(D) An error in recording.

Ans :

(C) An increase in the firm's recorded bank balance.
The debit side of the cash book's bank column is used to record all receipts and deposits. By debiting the account upon receiving a cheque, the accountant is recording an increase in the firm's assets as held by the bank, thus increasing the bank balance as per the firm's own records (the cash book).

Oct/Nov 2020

124. What is the primary reason for the time lag between a cheque being deposited by a trader and it being credited to his account by the bank?
(A) The bank is waiting for the trader's permission to credit the amount.
(B) The bank needs to physically transport the cash from the other bank.
(C) The bank charges a fee for immediate credit.
(D) The cheque needs to go through the clearing house process.

Ans :

(D) The cheque needs to go through the clearing house process.
When a cheque drawn on another bank is deposited, it must be sent through a clearing house. This process verifies the cheque's authenticity and ensures the paying bank has sufficient funds before transferring the money. This clearing cycle is the primary cause of the time lag between the date of deposit and the date of credit.

May/June 2022

125. Which of the following is a key difference between 'Entries which do not require change in Cashbook' and 'Entries which Require Change in Cashbook'?
(A) The former originate in the cash book, while the latter originate in the pass book.
(B) The former are errors, while the latter are timing differences.
(C) The former are large amounts, while the latter are small amounts.
(D) The former are always debits, while the latter are always credits.

Ans :

(A) The former originate in the cash book, while the latter originate in the pass book.
This is the fundamental distinction. 'Entries not requiring change' (like unpresented cheques) are recorded first by the firm in its cash book. 'Entries requiring change' (like bank charges) are transactions initiated by the bank and appear first in the pass book, requiring the firm to update its cash book accordingly.

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Oct/Nov 2023

126. A cheque of ₹ 350 was recorded twice on the credit side of the cash book. To correct this error in the adjusted cash book, what entry is required?
(A) A credit of ₹ 350. (B) A debit of ₹ 350.
(C) A debit of ₹ 700. (D) A credit of ₹ 700.

Ans :

(B) A debit of ₹ 350.
Recording the payment twice overstates the payments by ₹ 350 and understates the cash book balance by the same amount. To correct this, the extra payment entry must be reversed. Reversing a credit entry of ₹ 350 requires making a debit entry of ₹ 350, which will increase the balance back to its correct level.

Oct/Nov 2015

127. When a cheque is dishonoured, the bank debits the customer's account. The customer, in turn, must:
(A) Debit their cash book to reflect the failed deposit.
(B) Issue a new cheque to the bank.
(C) Wait for the bank to automatically correct the entry.
(D) Credit their cash book to reverse the original deposit entry.

Ans :

(D) Credit their cash book to reverse the original deposit entry.
The initial deposit was recorded with a debit to the cash book's bank column. The dishonour means this money was not actually received. To nullify the original entry and accurately reflect the failed transaction, the customer must make a credit entry in the cash book for the amount of the dishonoured cheque.

May/June 2010

128. If the cash book balance is taken as the starting point, which of the following items will be added to it to find the corrected cash book balance?
(A) Amount collected by the bank on standing instruction.
(B) Bank charges shown in the pass book only.
(C) Cheques issued but not yet presented for payment.
(D) Amounts paid by the bank on standing instruction.

Ans :

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(A) Amount collected by the bank on standing instruction.
An amount collected by the bank (like a dividend) on behalf of the firm increases the actual bank balance but may not yet be recorded in the cash book. This is an unrecorded receipt. To correct the cash book, this income must be added (debited) to the cash book balance to reflect the true financial position.

Oct/Nov 2022

129. The likelihood of clerical errors such as under casting or over casting is very low in which environment?
(A) A manual accounting system.
(B) A single-entry bookkeeping system.
(C) A computerised accounting environment.
(D) A system managed by a single accountant.

Ans :

(C) A computerised accounting environment.
In a computerised accounting system, calculations such as totaling (casting) columns are performed automatically by the software. This eliminates the human errors of incorrect addition or subtraction (under casting/overcasting) that are more common in manual systems, thus making the occurrence of such clerical errors very low.

May/June 2016

130. A debit balance in the cash book is ₹ 10,000. A credit balance in the pass book is ₹ 12,000. The only difference is bank charges. What is the amount of bank charges?
(A) ₹ 2,000
(B) ₹ 22,000
(C) ₹ 1,000
(D) Cannot be determined.

Ans :

(A) ₹ 2,000
Assuming the question intends to find the value of the reconciling item, the difference between the pass book balance (₹ 12,000) and the cash book balance (₹ 10,000) is ₹ 2,000. If this difference is solely due to a transaction recorded in one book but not the other, such as a direct deposit or interest credit, its value is ₹ 2,000. Note: The premise that the difference is 'bank charges' is conceptually flawed, as bank charges would make the pass book balance lower than the cash book balance, not higher.

CHAPTER 5

Trial Balance, Rectification of Errors & Adjusting & Closing Entries

May/June 2012

1. According to the principles of double-entry bookkeeping, what must be the relationship between total debits and total credits when a summary is prepared?
(A) Total debits must be greater than total credits.
(B) Total debits must tally with total credits.
(C) Total credits must be greater than total debits.
(D) The relationship is irrelevant for summary preparation.

Ans :

(B) Total debits must tally with total credits.
The double-entry system of bookkeeping is founded on the principle that every transaction has two aspects: a debit and a corresponding credit of an equal amount. Consequently, when a summary of all ledger account balances is prepared, the aggregate of all debit balances must equal the aggregate of all credit balances for the books to be arithmetically correct.

Oct/Nov 2016

2. Who defines a Trial Balance as "a list or abstract of balances or of total debits and total credits of the accounts in a ledger the purpose being to determine the equality of posted debits and credits"?
(A) Eric L. Kohler
(B) Mr. Carter
(C) The Institute of Chartered Accountants
(D) The American Institute of Certified Public Accountants

Ans :

(A) Eric L. Kohler
In his work, The Directory for Accountants, Eric L. Kohler provides a formal definition of a Trial Balance. He describes it as a list or abstract of account balances or totals, primarily created to verify the arithmetical equality of debits and credits posted in the ledger and to serve as a foundational summary for preparing financial statements.

May/June 2021

3. As per Mr. Carter's definition, in addition to debit and credit balances from the ledger, what other balances are included in a Trial Balance?
(A) Only balances of personal accounts.
(B) Only balances of nominal accounts.
(C) Balances of cash in hand and cash at bank.
(D) Balances of contingent liabilities and assets.

Ans :

(C) Balances of cash in hand and cash at bank.
Mr. Carter's definition specifies that a Trial Balance is a list of debit and credit balances extracted from various ledger accounts. Crucially, it also explicitly includes the balances of cash in hand and cash at bank, as shown by the cash book, to provide a complete summary of all account balances on a particular date.

Oct/Nov 2005

4. What is the primary purpose of preparing a Trial Balance?
(A) To calculate the net profit or loss for the period.
(B) To ascertain the financial position of the business.
(C) To serve as a book of original entry.
(D) To establish the arithmetical accuracy of transactions recorded.

Ans :

(D) To establish the arithmetical accuracy of transactions recorded.
The main objective of a Trial Balance is to verify the arithmetical correctness of the posting and balancing of ledger accounts. By confirming that the total of all debit balances equals the total of all credit balances, it provides a preliminary check on the accuracy of the bookkeeping process before the preparation of the final financial statements.

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May/June 2015

5. Which of the following statements about the features of a Trial Balance is incorrect?
(A) It is a list of debit and credit balances drawn from the ledger.
(B) It facilitates the preparation of final accounts.
(C) It is only prepared at the end of the financial year.
(D) It includes cash and bank balances.

Ans :

(C) It is only prepared at the end of the financial year.
While a Trial Balance is commonly prepared at the end of a financial year, it is not restricted to that timing. It can be prepared at any time as required, such as monthly, quarterly, or half-yearly, to check the arithmetical accuracy of the books of account at more frequent intervals.

Oct/Nov 2023

6. How does a Trial Balance assist a trader in managing receivables and payables?
(A) By directly calculating the collection period for all debtors.
(B) By enabling the trader to know the total amounts receivable and payable.
(C) By showing the total profit generated from individual customers.
(D) By automatically sending payment reminders to overdue customers.

Ans :

(B) By enabling the trader to know the total amounts receivable and payable.
The Trial Balance lists the balances of all ledger accounts, including those of individual customers (debtors) and suppliers (creditors). This allows the trader to easily see the total amount receivable from all customers and the total amount payable to all suppliers at a specific point in time, aiding in the management of working capital.

May/June 2008

7. What are the two types of trial balance mentioned in the chapter?
(A) Detailed trial balance and Summary trial balance.
(B) Interim trial balance and Final trial balance.
(C) Manual trial balance and Computerized trial balance.
(D) Gross trial balance and Net trial balance.

Ans :

(D) Gross trial balance and Net trial balance.
The text explicitly identifies two types of trial balance that can be prepared from the ledger accounts. These are the Gross trial balance, which lists the total debits and total credits of each account, and the Net trial balance, which lists only the final debit or credit balance of each account.

Oct/Nov 2011

8. What is the first step in preparing a Gross Trial Balance?
(A) Take totals of debit and credit columns of each ledger account.
(B) Write the names of all accounts in a statement format.
(C) Enter the net balance against each individual item.
(D) Take the total of the debit and credit columns of the trial balance.

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Ans :

(A) Take totals of debit and credit columns of each ledger account.
The preparation of a Gross Trial Balance begins at the ledger level. The very first stage involves calculating the total of the debit side and the total of the credit side for every single account maintained in the ledger. These totals, rather than the net balances, form the basis of the Gross Trial Balance.

May/June 2018

9. In a Gross Trial Balance, what figures are entered against the name of each account?
(A) The net debit or credit balance of the account.
(B) The opening balance of the account from the previous period.
(C) The total of the debit column and the total of the credit column.
(D) The final closing balance of the account for the period.

Ans :

(C) The total of the debit column and the total of the credit column.
Unlike a Net Trial Balance which shows only the final balance, a Gross Trial Balance presents the gross totals for each account. For every account listed, the statement shows the total of all debit entries in one column and the total of all credit

entries in another column, directly reflecting the ledger totals.

Oct/Nov 2014

10. Based on the data provided in Illustration No. 1 for Mr. Bhagwandas, what are the total debit and credit amounts for the 'Purchases' account?
(A) Debit ₹1,90,000; Credit ₹4,000
(B) Debit ₹1,90,000; Credit ₹18,000
(C) Debit ₹1,90,000; Credit ₹2,45,000
(D) Debit ₹4,000; Credit ₹1,90,000

Ans :

(A) Debit ₹1,90,000; Credit ₹4,000
The table in Illustration No. 1 presents the totals of the debit and credit sides for various ledger accounts. By locating the 'Purchases' account in the list, the corresponding figures are a total debit side of ₹1,90,000 and a total credit side of ₹4,000. These figures would be used to prepare the Gross Trial Balance.

May/June 2005

11. According to the data in Illustration No. 1, what are the total debit and credit amounts for the 'Sales' account?
(A) Debit ₹13,000; Credit ₹2,45,000
(B) Debit ₹2,45,000; Credit ₹6,000
(C) Debit ₹6,000; Credit ₹18,000
(D) Debit ₹6,000; Credit ₹2,45,000

Ans :

(D) Debit ₹6,000; Credit ₹2,45,000
The table for Mr. Bhagwandas as on 31st March 2022 provides the total debit and credit side for each account. For the 'Sales' account, the table explicitly states that the total of the debit side is ₹6,000, and the total of the credit side is ₹2,45,000.

Oct/Nov 2009

12. From Illustration No. 1, which account has a debit side total of ₹3,05,000 and a credit side total of ₹2,50,000?
(A) Suppliers
(B) Customers
(C) XYZ Bank
(D) Sales

Ans :

(B) Customers
By examining the provided table in Illustration No. 1, we can identify the account that matches the given totals. The 'Customers' account is listed with a 'Total of debit side' of ₹3,05,000 and a 'Total of credit side' of ₹2,50,000, representing total sales to and total receipts from customers respectively.

May/June 2023

13. What is the total of the debit and credit columns in the Gross Trial Balance of Mr. Bhagwandas as on 31st March 2022?
(A) ₹4,17,000
(B) ₹10,00,000
(C) ₹12,00,000
(D) ₹2,81,000

Ans :

(C) ₹12,00,000
The solution provided for Illustration No. 1 shows the completed Gross Trial Balance. After listing the total debit and total credit for each individual account from the ledger, the final step is to sum these two columns. The summation reveals that both the debit column and the credit column total ₹12,00,000, indicating arithmetical accuracy.

Oct/Nov 2018

14. How is a Net Trial Balance different from a Gross Trial Balance?
(A) It shows the total debits and total credits for each account.
(B) It is prepared more frequently than a Gross Trial Balance.
(C) It entirely excludes cash and bank balance accounts.
(D) It shows only the net debit or credit balance of each account.

Ans :

(D) It shows only the net debit or credit balance of each account.
The fundamental difference lies in how account information is presented. A Gross Trial Balance lists the total debits and total credits for every account. In contrast, a Net Trial Balance is more concise, showing only the final net balance of each account, which will be either a debit balance or a credit balance.

May/June 2007

15. Using the data from Illustration No. 1, what is the net balance of the 'Bhagwandas Capital' account to be shown in the Net Trial Balance?
(A) ₹1,25,000 Credit
(B) ₹1,25,000 Debit

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(C) ₹1,35,000 Credit
(D) ₹10,000 Debit

Ans :

(A) ₹1,25,000 Credit
The Gross Trial Balance data shows 'Bhagwandas Capital' with a credit total of ₹1,35,000 and a debit total of ₹10,000. The net balance is the difference between the two sides. Since the credit side is larger, the net balance is a credit of ₹1,35,000 - ₹10,000 = ₹1,25,000. This is confirmed in the Net Trial Balance solution.

Oct/Nov 2025

16. What is the net debit balance of the 'Purchases' account in the Net Trial Balance of Mr. Bhagwandas?
(A) ₹1,90,000
(B) ₹1,86,000
(C) ₹1,94,000
(D) ₹4,000

Ans :

(B) ₹1,86,000
The gross figures for the Purchases account are Debit ₹1,90,000 and Credit ₹4,000. To find the net balance, we subtract the smaller side from the larger side.
The debit side is larger, so the net balance is a debit of ₹1,90,000 - ₹4,000 = ₹1,86,000.
This is the figure that appears in the Net Trial Balance.

May/June 2019

17. In the Net Trial Balance of Mr. Bhagwandas, what is the net balance for the 'Customers' account?
(A) ₹55,000 Credit
(B) ₹55,000 Debit
(C) ₹3,05,000 Debit
(D) ₹2,50,000 Credit

Ans :

(B) ₹55,000 Debit
The gross totals for the 'Customers' account are Debit ₹3,05,000 and Credit ₹2,50,000. The debit side represents sales to customers, and the credit side represents payments received. The net debit balance, representing the amount still receivable, is ₹3,05,000 - ₹2,50,000 = ₹55,000. This is correctly shown as a debit balance in the Net Trial Balance.

Oct/Nov 2006

18. Calculate the net balance of the 'XYZ Bank' account from the data provided for Mr. Bhagwandas.
(A) ₹6,000 Debit
(B) ₹6,000 Credit
(C) ₹2,81,000 Debit
(D) ₹2,75,000 Credit

Ans :

(A) ₹6,000 Debit
For the 'XYZ Bank' account, the total of the debit side (receipts/deposits) is ₹2,81,000, and the total of the credit side (payments) is ₹2,75,000. Since the debit total is greater than the credit total, the account has a net debit balance of ₹2,81,000 - ₹2,75,000 = ₹6,000, representing cash at bank.

May/June 2016

19. What is the final total of the debit and credit columns in the Net Trial Balance prepared for Mr. Bhagwandas?
(A) ₹12,00,000
(B) ₹5,00,000
(C) ₹4,17,000
(D) ₹3,50,000

Ans :

(C) ₹4,17,000
The solution for Illustration No. 1 presents the completed Net Trial Balance. After calculating and listing the net debit or credit balance for each account, the two columns are totalled. The sum of the debit column and the sum of the credit column both amount to ₹4,17,000, confirming the arithmetical accuracy of the ledger balances.

Oct/Nov 2010

20. According to the principle stated before Illustration No. 2, which types of accounts normally show debit balances in a trial balance?
(A) Assets and expenses accounts
(B) Incomes and liabilities accounts
(C) Capital and liabilities accounts
(D) Incomes and gains accounts

Ans :

(A) Assets and expenses accounts
The text provides a fundamental rule for preparing a trial balance: assets and expenses accounts show debit balances. Assets represent resources owned by the business, and expenses represent costs incurred. Following the rules of debit and

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credit, these accounts naturally accumulate debit balances, which are then reflected in the trial balance debit column.

May/June 2016

21. Following the principle stated before Illustration No. 2, which types of accounts typically show credit balances?
(A) Assets and expenses accounts
(B) Drawings and losses accounts
(C) Incomes and liabilities accounts
(D) Purchases and returns inward accounts

Ans :

(C) Incomes and liabilities accounts
The guiding principle mentioned is that incomes and liabilities accounts show credit balances in the trial balance. Liabilities represent obligations to external parties, and incomes represent earnings or gains. As per accounting rules, increases in liabilities and incomes are credited, leading to them normally having credit balances at the end of an accounting period.

Oct/Nov 2022

22. In Illustration No. 2 for Shri Inderkumar, how should 'Bank Overdraft' of ₹5,000 be treated in the Trial Balance?
(A) As a debit balance, because bank accounts are typically assets.
(B) It should be deducted from the Cash in Hand balance.
(C) It should be ignored as it is not an asset or expense.
(D) As a credit balance, because it is a liability to the bank.

Ans :

(D) As a credit balance, because it is a liability to the bank.
A bank overdraft represents a situation where more money has been withdrawn than was available in the account, creating a loan from the bank. It is a liability for the business. According to the accounting principle that liabilities have credit balances, the Bank Overdraft amount of ₹5,000 must be placed in the credit column of the Trial Balance.

May/June 2018

23. From the balances of Shri Inderkumar in Illustration No. 2, how would 'Loan from X' (₹8,000) and 'Loan to Y' (₹3,000) be placed in the Trial Balance?
(A) Both as debit balances, as they are loan accounts.
(B) Both as credit balances, as they involve external parties.
(C) 'Loan from X' as debit, 'Loan to Y' as credit.
(D) 'Loan from X' as credit, 'Loan to Y' as debit.

Ans :

(D) 'Loan from X' as credit, 'Loan to Y' as debit.
'Loan from X' is a liability, representing money borrowed by the business, and liabilities have credit balances. Therefore, ₹8,000 is a credit. 'Loan to Y' is an asset, representing money lent by the business to an external party, and assets have debit balances. Therefore, ₹3,000 is a debit.

Oct/Nov 2016

24. What is the total of the debit and credit columns in the Trial Balance of Shri Inderkumar as on 31st March, 2022?
(A) ₹55,000
(B) ₹50,000
(C) ₹45,000
(D) ₹60,000

Ans :

(B) ₹50,000
By correctly classifying each item from Illustration No. 2 into the debit or credit column and then summing them up, the final totals are determined. The solution shows that after placing all assets and expenses on the debit side and all liabilities, capital, and incomes on the credit side, both columns correctly total to ₹50,000.

May/June 2014

25. What is the primary reason for the disagreement of a Trial Balance?
(A) The business is consistently running at a loss.
(B) The use of the double-entry system causes complexity.
(C) Errors committed during journalising and posting.
(D) Preparation of the trial balance at the year-end.

Ans :

(C) Errors committed during journalising and posting.
A Trial Balance is designed to verify arithmetical accuracy. If it does not tally, it signifies that one

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or more errors have occurred in the accounting process. These mistakes can happen during the initial recording of transactions in journals (journalising) or when transferring those entries to the respective ledger accounts (posting), disrupting the equality of debits and credits.

Oct/Nov 2007

26. Which of the following is a key characteristic of certain errors that are not disclosed even when a Trial Balance agrees?

(A) They always involve incorrect monetary amounts.
(B) They are always classified as errors of principle.
(C) They only occur in subsidiary books of entry.
(D) They affect both debit and credit aspects equally.

Ans :

(D) They affect both debit and credit aspects equally.
The agreement of a Trial Balance only confirms the equality of total debits and total credits. It does not guarantee freedom from all errors. Certain errors, such as completely omitting a transaction or posting a correct amount to the wrong account, do not cause an imbalance because the debit and credit sides are still equally affected.

May/June 2025

27. Errors in accounting can be broadly divided into which two main types?

(A) One-sided errors and Two-sided errors.
(B) Errors of Omission and Errors of Commission.
(C) Arithmetical errors and Non-arithmetical errors.
(D) Clerical errors and Principle errors.

Ans :

(D) Clerical errors and Principle errors.
The chapter provides a broad classification of accounting errors into two primary categories. The first is 'Clerical errors', which are mistakes made in the routine process of recording and posting. The second is 'Errors of Principle', which involve a violation of fundamental accounting principles, such as treating a capital expenditure as a revenue expenditure.

Oct/Nov 2019

28. Which of the following is not a sub-division of Clerical Errors?

(A) Errors of principle
(B) Errors of omission
(C) Errors of commission
(D) Compensating errors

Ans :

(A) Errors of principle
Clerical errors are further categorized into three types: Errors of Omission (forgetting to record), Errors of Commission (making a mistake while recording), and Compensating Errors (one error cancels out another). Errors of Principle are a separate main category of error, distinct from clerical errors, as they relate to the incorrect application of accounting rules.

May/June 2009

29. Consider the following description: "When a transaction is completely or partially omitted to be recorded in books of account, it is called an 'Error of omission'". Which of the following best exemplifies a 'Partial omission'?

(A) A credit purchase from Mr. A is not recorded in the purchase journal.
(B) A credit sale to Mr. B is not recorded in the sales journal.
(C) A purchase entry is recorded in the journal but not posted to the supplier's account.
(D) A cash payment for rent is not recorded anywhere.

Ans :

(C) A purchase entry is recorded in the journal but not posted to the supplier's account.
A partial omission occurs when one aspect of a double-entry is recorded, but the other is not. Recording the purchase in the journal correctly affects the purchase account, but failing to post it to the supplier's account leaves the double entry incomplete. This affects only one account in the ledger, causing the trial balance to disagree.

Oct/Nov 2011

30. How does a 'Complete omission' affect the Trial Balance?

(A) It causes the debit side of the trial balance to be higher.
(B) It does not affect the agreement of the Trial Balance.
(C) It causes the credit side of the trial balance to be higher.
(D) It doubles the difference in the totals of the Trial Balance.

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Ans :

(B) It does not affect the agreement of the Trial Balance.

An error of complete omission means that the entire transaction, including both its debit and credit aspects, has been left out of the books of account. Since neither a debit nor a credit has been recorded for the transaction, the fundamental equality of total debits and total credits remains undisturbed, and the Trial Balance will still agree.

May/June 2010

31. Which of the following is an example of an 'Error of Commission'?

(A) Wages paid for the installation of machinery are debited to the Wages Account.
(B) A credit sale of ₹5,000 is completely omitted from the books.
(C) Rent account is undercast by ₹500 and salary account is overcast by ₹500.
(D) A credit sale of ₹720 to Mr. Sanjay is posted to his account as ₹270.

Ans :

(D) A credit sale of ₹720 to Mr. Sanjay is posted to his account as ₹270.

An error of commission occurs when a transaction is recorded with a wrong amount, on the wrong side, or in the wrong account. Posting a correct sale of ₹720 as ₹270 is a clear example of posting a wrong amount on the correct side of the correct account, which falls under the category of an error of commission.

Oct/Nov 2024

32. If a correct amount is posted to the correct account but on the wrong side (e.g., a debit posted as a credit), what type of error is this?

(A) Error of Omission
(B) Error of Commission
(C) Error of Principle
(D) Compensating Error

Ans :

(B) Error of Commission

Errors of commission encompass various procedural mistakes in recording or posting. Posting an amount to the wrong side of an account is a specific type of commission error. This action violates the correct double-entry procedure, even if the amount and account are correct, and will cause the trial balance to disagree.

May/June 2017

33. An amount of ₹2,000 received from a customer, Ramesh, was correctly recorded in the cash book but was posted to the debit side of Ramesh's account. What is the consequence of this error?

(A) The Trial Balance will still agree due to the cash book entry.
(B) The Trial Balance will show an excess credit of ₹4,000.
(C) The Trial Balance will show an excess debit of ₹4,000.
(D) It will be classified as an error of principle, not commission.

Ans :

(C) The Trial Balance will show an excess debit of ₹4,000.

Cash received (₹2,000) should be credited to the customer's account. By incorrectly debiting it, the debit side is overstated by ₹2,000 and the credit side is understated by ₹2,000. The total difference is an excess debit of ₹4,000. This is an error of commission (posting to the wrong side).

Oct/Nov 2005

34. What defines a 'Compensating Error'?

(A) An error that violates fundamental accounting principles.
(B) An error where a transaction is completely omitted from records.
(C) An error where one mistake's effect is nullified by another mistake.
(D) An error of posting the wrong amount to the correct ledger account.

Ans :

(C) An error where one mistake's effect is nullified by another mistake.

A compensating error involves two or more independent mistakes that, by coincidence, cancel each other out. For example, if one expense account is undercast by ₹1,000 and another expense account is overcast by ₹1,000, the net effect on the trial balance totals is zero, so the trial balance will still agree despite the errors.

May/June 2020

35. Which of the following scenarios describes a compensating error?

(A) Rent account is undercast by ₹1,000, and the printing account is overcast by ₹1,000.
(B) Purchase of goods worth ₹5,000 not recorded in the books.

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(C) Purchase of furniture for ₹10,000 debited to the purchases account.
(D) Sales account total is overcast by ₹500, and the purchases account total is undercast by ₹500.

Ans :

(A) Rent account is undercast by ₹1,000, and the printing account is overcast by ₹1,000.
In this case, the rent account (an expense) has a debit balance that is ₹1,000 too low. The printing account (another expense) has a debit balance that is ₹1,000 too high. The understatement of one debit is exactly offset by the overstatement of another debit, so the total of the trial balance debit column remains correct.

Oct/Nov 2015

36. Debiting wages paid for the installation of machinery to the wages account instead of the machinery account is an example of what type of error?
(A) Error of Omission
(B) Error of Principle
(C) Error of Commission
(D) Compensating Error

Ans :

(B) Error of Principle
This error involves a violation of the accounting principle that costs incurred to make an asset ready for use should be capitalized (added to the asset's cost). By treating a capital expenditure (installation of machinery) as a revenue expenditure (wages), a fundamental principle has been broken. The trial balance will still agree, but profit and asset values will be incorrect.

May/June 2013

37. How do errors of principle typically affect the agreement of the Trial Balance?
(A) They always cause the debit side of the trial balance to be higher.
(B) They always cause the credit side of the trial balance to be higher.
(C) The effect depends entirely on the amount of the transaction.
(D) They do not affect the agreement of the Trial Balance.

Ans :

(D) They do not affect the agreement of the Trial Balance.
Errors of principle involve recording a transaction in the wrong class of account (e.g., revenue vs. capital) but still adhering to the double-entry rule of debit and credit. For instance, debiting an expense instead of an asset still results in a valid debit entry. Therefore, the equality of debits and credits is maintained, and the trial balance agrees.

Oct/Nov 2021

38. The provided chart classifies errors into various types. According to this chart, which of the following errors affects the trial balance?
(A) Errors of Commission
(B) Errors of Principle
(C) Complete Errors of Omission
(D) Compensating Errors

Ans :

(A) Errors of Commission
The diagram clearly shows the impact of different error types. 'Errors of Principle', 'Compensating Errors', and 'Complete' Errors of Omission are all shown with the note '(No effect on trial balance)'. In contrast, 'Errors of Commission' and 'Partial' Errors of Omission are shown with the note '(Affect trial balance)', indicating they cause a disagreement.

May/June 2024

39. As per the diagram on error classification, which three sub-types of errors fall under 'Clerical Errors'?
(A) Errors of Principle, Errors of Omission, and Errors of Commission.
(B) Errors of Omission and Errors of Commission.
(C) Errors of Omission, Errors of Commission, and Compensating Errors.
(D) Errors of Commission and Compensating Errors.

Ans :

(C) Errors of Omission, Errors of Commission, and Compensating Errors.
The chart displays a hierarchical structure. 'Types of Errors' branches into 'Errors of Principle' and 'Clerical Errors'. The 'Clerical Errors' branch further splits into three distinct categories: 'Errors of Omission', 'Errors of Commission', and 'Compensating Errors', showing that all three are considered types of clerical mistakes.

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Oct/Nov 2008

40. The first step suggested to locate an error when a trial balance disagrees is to:
(A) Re-check the totals of the debit and credit sides of the trial balance.
(B) Verify the cash and bank balances against the cash book.
(C) Divide the difference by two to check for wrong-side postings.
(D) Look for a transaction of an amount equal to the difference.

Ans :

(A) Re-check the totals of the debit and credit sides of the trial balance.
The most basic potential mistake is a simple addition error in the trial balance itself. Therefore, the logical first step in troubleshooting a disagreement is to re-calculate the totals of the debit and credit columns to ensure they have been summed up correctly before proceeding to more complex checks of the underlying accounting records.

May/June 2006

41. A trial balance shows a difference where the debit side is in excess by ₹1,600. According to the steps for locating errors, what does taking half the amount of the difference (i.e., ₹800) help to identify?
(A) An item of ₹800 was omitted from the credit side.
(B) An item of ₹1,600 was posted twice on the debit side.
(C) A credit item of ₹800 was wrongly posted to the debit side.
(D) A debit item of ₹800 was posted twice to the same account.

Ans :

(C) A credit item of ₹800 was wrongly posted to the debit side.
If a credit item of ₹800 is wrongly placed on the debit side, it causes two problems: the credit side is understated by ₹800, and the debit side is overstated by ₹800. The total difference between the two sides becomes ₹1,600. Therefore, halving the total difference helps to identify the amount of a transaction posted to the wrong side.

Oct/Nov 2017

42. One-sided errors located before preparing a trial balance are rectified by:
(A) Passing a formal rectification journal entry.
(B) Simply making a corrective posting in the affected ledger account.
(C) Preparing a suspense account to hold the error amount.
(D) Informing the auditors for external verification.

Ans :

(B) Simply making a corrective posting in the affected ledger account.
When a one-sided error (an error affecting only one account) is found before the trial balance is drawn up, the ledger is still open and being worked on. The simplest and most direct way to rectify it is to make the correction directly in the affected ledger account with an explanatory note, without needing a formal journal entry.

May/June 2008

43. In Illustration No. 3, rent paid of ₹90 was incorrectly posted as ₹900. How is this one-sided error rectified before the preparation of a trial balance?
(A) Debit Rent a/c with ₹810.
(B) Pass a journal entry: Cash a/c Dr. ₹810 to Rent a/c ₹810.
(C) Credit Rent a/c with the words 'By excess debit ₹810'.
(D) Pass a journal entry: Suspense a/c Dr. ₹810 to Rent a/c ₹810.

Ans :

(C) Credit Rent a/c with the words 'By excess debit ₹810'.
The rent account was debited with ₹900 instead of the correct ₹90. This is an excess debit of ₹810. To correct this one-sided error before a trial balance, no formal journal entry is needed. The correction is made by simply posting a credit of ₹810 to the Rent account with an appropriate narration like 'By excess debit'.

Oct/Nov 2013

44. The sales register was undercasted by ₹100, as mentioned in Illustration No. 3. What is the appropriate rectification for this one-sided error before preparing the trial balance?
(A) Debit the Sales account with 'To under casting ₹100'.
(B) Pass a journal entry: Suspense a/c Dr. ₹100 to Sales a/c ₹100.
(C) Deduct ₹100 from the total of the Customers'

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account.
(D) Credit the Sales account with the words 'By under casting ₹100'.

Ans :

(D) Credit the Sales account with the words 'By under casting ₹100'.
Undercasting the sales register means the total sales credit is ₹100 less than it should be. The total is posted to the credit of the Sales account. To correct this one-sided error, the Sales account needs to be credited by the short amount. This is done by making a credit entry of ₹100 with a narration like 'By under casting'.

May/June 2015

45. An amount of ₹200 received from Suresh was wrongly posted to his debit. What is the effect of this error and what is the rectification amount?
(A) The difference will be ₹400; credit Suresh's a/c with ₹400.
(B) The difference will be ₹200; credit Suresh's a/c with ₹200.
(C) The difference will be ₹200; debit Suresh's a/c with ₹200.
(D) The difference will be ₹400; debit Suresh's a/c with ₹400.

Ans :

(A) The difference will be ₹400; credit Suresh's a/c with ₹400.
A receipt from Suresh should have been a ₹200 credit to his account. Posting it as a ₹200 debit makes his account balance incorrect by double the amount (the missing ₹200 credit plus the incorrect ₹200 debit). To rectify this, Suresh's account must be credited with ₹400 to cancel the wrong debit and establish the correct credit.

Oct/Nov 2012

46. What characterizes a 'two-sided error'?
(A) It affects only one ledger account.
(B) Two or more ledger accounts are affected incorrectly.
(C) It is rectified without passing a formal journal entry.
(D) It never affects the trial balance agreement.

Ans :

(B) Two or more ledger accounts are affected incorrectly.
Unlike a one-sided error that impacts a single ledger account, a two-sided error involves incorrect entries in two or more accounts. Rectifying such errors requires a formal journal entry to correct the debit and credit effects across all the affected accounts, ensuring the accounting equation remains in balance after the correction.

May/June 2011

47. The text describes a procedure for rectifying two-sided errors. What is the recommended first step in this process?
(A) Compare the wrong entry with the correct one to find the difference.
(B) Pass the final rectification entry immediately.
(C) Analyze and show the wrong entry which is already passed.
(D) Determine and write down the correct entry that should have been passed.

Ans :

(D) Determine and write down the correct entry that should have been passed.
The text outlines a systematic approach to rectifying two-sided errors. The process begins by first determining and writing down the correct journal entry for the transaction as it should have been recorded. This establishes a clear baseline against which the incorrect entry can be compared to identify the necessary corrections.

Oct/Nov 2020

48. In Illustration 4, goods purchased from Sohanlal for ₹500 were wrongly recorded in the sales register. What is the correct rectification entry?
(A) Sales a/c Dr. ₹500; Purchase a/c Dr. ₹500; To Sohanlal a/c ₹1,000.
(B) Sohanlal a/c Dr. ₹1,000; To Sales a/c ₹500; To Purchases a/c ₹500.
(C) Sales a/c Dr. ₹500; To Purchases a/c ₹500.
(D) Purchases a/c Dr. ₹500; To Sales a/c ₹500.

Ans :

(A) Sales a/c Dr. ₹500; Purchase a/c Dr. ₹500; To Sohanlal a/c ₹1,000.
The wrong entry was Sohanlal Dr. 500 to Sales Cr. 500. The correct entry should have been Purchases Dr. 500 to Sohanlal Cr. 500. To rectify: (1) Debit Purchases a/c for ₹500 to record the purchase. (2) Debit Sales a/c for ₹500 to cancel the wrong credit. (3) Credit Sohanlal a/c for ₹1,000 to reverse the wrong debit and give the correct credit.

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May/June 2022

49. Salary of ₹1,000 paid to Vijay, an accountant, was wrongly debited to his personal account. What is the rectification entry?
(A) Salary a/c Dr. ₹1,000; To Cash a/c ₹1,000.
(B) Vijay a/c Dr. ₹1,000; To Salary a/c ₹1,000.
(C) Salary a/c Dr. ₹1,000; To Vijay a/c ₹1,000.
(D) Suspense a/c Dr. ₹1,000; To Vijay a/c ₹1,000.

Ans :

(C) Salary a/c Dr. ₹1,000; To Vijay a/c ₹1,000.
The wrong entry debited Vijay's personal account instead of the Salary account. The correct entry should have debited the Salary account. To rectify this, the Salary account must be debited to record the expense correctly, and Vijay's personal account must be credited to cancel the incorrect debit that was posted to it.

Oct/Nov 2023

50. Wages of ₹500 paid for the installation of machinery were debited to the wages account. This is an error of principle. What is the correct rectification entry?
(A) Machinery a/c Dr. ₹500; To Wages a/c ₹500.
(B) Wages a/c Dr. ₹500; To Machinery a/c ₹500.
(C) Machinery a/c Dr. ₹500; To Cash a/c ₹500.
(D) Profit & Loss Adjustment a/c Dr. ₹500; To Wages a/c ₹500.

Ans :

(A) Machinery a/c Dr. ₹500; To Wages a/c ₹500.
This error incorrectly treated a capital expenditure as a revenue expense. To rectify, the Machinery account (an asset) must be debited to capitalize the cost. The Wages account, which was wrongly debited, must be credited to cancel the incorrect expense booking. This correctly moves the amount from an expense account to an asset account.

May/June 2016

51. Rent paid of ₹200 was correctly entered in the cash book but wrongly debited to the postage account during ledger posting. Identify the rectification entry.
(A) Rent a/c Dr. ₹200; To Cash a/c ₹200.
(B) Postage a/c Dr. ₹200; To Rent a/c ₹200.
(C) Suspense a/c Dr. ₹200; To Postage a/c ₹200.
(D) Rent a/c Dr. ₹200; To Postage a/c ₹200.

Ans :

(D) Rent a/c Dr. ₹200; To Postage a/c ₹200.
An error was made during posting from the cash book. The debit should have gone to the Rent account but was incorrectly sent to the Postage account. To correct this, the Rent account must be debited to record the expense properly. Simultaneously, the Postage account must be credited to reverse the incorrect debit it received.

Oct/Nov 2009

52. When is a 'Suspense' account typically opened?
(A) At the beginning of every financial year as a standard practice.
(B) When a trial balance disagrees, to temporarily hold the difference.
(C) To record all transactions of a temporary or uncertain nature.
(D) To specifically rectify all errors of principle found in the books.

Ans :

(B) When a trial balance disagrees, to temporarily hold the difference.
A Suspense account is a temporary account used by accountants to make the trial balance agree when its totals do not match. The difference between the debit and credit totals is placed in the suspense account, allowing for the preparation of financial statements while the underlying errors are located and rectified at a later stage.

May/June 2023

53. If one-sided errors are found after the preparation of a trial balance and the difference has been moved to a suspense account, how are they rectified?
(A) By correcting the posting directly in the ledger without a journal entry.
(B) They cannot be rectified until the start of the next financial year.
(C) A journal entry is passed where the second account is the suspense account.
(D) A journal entry is passed using the Profit and Loss Adjustment account.

Ans :

(C) A journal entry is passed where the second account is the suspense account.
Once a suspense account holds the trial balance difference, any one-sided error discovered must be rectified using a journal entry. Since a one-sided error affects only one account, the suspense account itself serves as the other side of the entry

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to complete the double-entry requirement for the rectification, thereby reducing its own balance.

Oct/Nov 2018

54. If the debit total of a trial balance is more than the credit total, where is the difference placed in the suspense account?
(A) On the debit side of the suspense account.
(B) It is carried forward without being placed in any account.
(C) It is immediately debited to the Profit & Loss account.
(D) On the credit side of the suspense account.

Ans :

(D) On the credit side of the suspense account.
To make the trial balance totals equal, the suspense account is used to balance them. If the debit total is higher, it means the trial balance is short on the credit side. Therefore, the difference is placed on the credit side of the suspense account, which is then added to the credit column of the trial balance to make it tally.

May/June 2007

55. If a balance remains in the 'Suspense a/c' at the time of preparing final accounts, where is a debit balance in the suspense account shown?
(A) On the asset side of the Balance Sheet.
(B) On the credit side of the Trading Account.
(C) On the liability side of the Balance Sheet.
(D) As a direct deduction from the Capital account.

Ans :

(A) On the asset side of the Balance Sheet.
If, after all efforts, errors cannot be located and a balance persists in the suspense account, it must be shown in the Balance Sheet. A debit balance in the suspense account is treated as an unclassified asset and is therefore shown on the asset side of the Balance Sheet pending future investigation and clearance.

Oct/Nov 2025

56. In Illustration No. 5, the trial balance of Mr. Gidwani was out by ₹763 excess credit. How would this initial difference be recorded in the Suspense Account?
(A) As 'By Balance b/d' ₹763 on the credit side.
(B) As 'To Balance b/d' ₹763 on the debit side.
(C) As 'To Profit & Loss A/c' ₹763 on the debit side.
(D) It would not be recorded until all rectification entries are passed.

Ans :

(B) As 'To Balance b/d' ₹763 on the debit side.
An excess credit in the trial balance means the debit side is short by ₹763. To make the trial balance agree, a debit of ₹763 is needed. This amount is placed on the debit side of the Suspense Account. Therefore, the opening entry in the Suspense Account ledger would be 'To Balance b/d' for ₹763.

May/June 2012

57. An amount of ₹150 received from Bhagatram was completely omitted from the cash book. What is the rectification entry for this total omission?
(A) Suspense a/c Dr. ₹150; To Bhagatram ₹150.
(B) Bhagatram Dr. ₹150; To Cash a/c ₹150.
(C) Cash a/c Dr. ₹150; To Suspense a/c ₹150.
(D) Cash a/c Dr. ₹150; To Bhagatram ₹150.

Ans :

(D) Cash a/c Dr. ₹150; To Bhagatram ₹150.
This is an error of complete omission, meaning the entire transaction was unrecorded. It affects two accounts (Cash and Bhagatram) and does not impact the trial balance agreement or the suspense account. The rectification is simply to pass the correct journal entry that was originally missed: debit Cash a/c and credit Bhagatram's account.

Oct/Nov 2014

58. The total of the return inward book was cast short by ₹251. This is a one-sided error. What is the rectification entry using the Suspense Account?
(A) Sales Return a/c Dr. ₹251; To Suspense a/c ₹251.
(B) Suspense a/c Dr. ₹251; To Sales Return a/c ₹251.
(C) Customers a/c Dr. ₹251; To Suspense a/c ₹251.
(D) Sales Return a/c Dr. ₹251; To Customers a/c ₹251.

Ans :

(A) Sales Return a/c Dr. ₹251; To Suspense a/c ₹251.
The Return Inward (Sales Return) account, which should have a debit balance, is understated by ₹251 due to the short casting (undercasting). To correct this, the Sales Return account must be

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debited by ₹251. Since this is a one-sided error discovered after creating the suspense account, the corresponding credit is posted to the Suspense account.

May/June 2019

59. A purchase of ₹68 had been posted to the creditor's account as ₹60. What is the rectification entry for this short credit?
(A) Creditors a/c Dr. ₹8; To Suspense a/c ₹8.
(B) Purchases a/c Dr. ₹8; To Suspense a/c ₹8.
(C) Suspense a/c Dr. ₹8; To Creditors a/c ₹8.
(D) Suspense a/c Dr. ₹68; To Creditors a/c ₹68.

Ans :

(C) Suspense a/c Dr. ₹8; To Creditors a/c ₹8.
The creditor's account should have been credited with ₹68 but was only credited with ₹60, a short credit of ₹8. This is a one-sided posting error. To rectify it, the creditor's account needs to be credited by the difference of ₹8. The corresponding debit to complete the journal entry is made to the Suspense account.

Oct/Nov 2006

60. A sale of ₹260 to Uday Traders was wrongly credited to their account. What is the correct rectification entry and the amount involved?
(A) Uday Traders a/c Dr. ₹520; To Suspense a/c ₹520.
(B) Uday Traders a/c Dr. ₹260; To Suspense a/c ₹260.
(C) Suspense a/c Dr. ₹260; To Uday Traders a/c ₹260.
(D) Suspense a/c Dr. ₹520; To Uday Traders a/c ₹520.

Ans :

(A) Uday Traders a/c Dr. ₹520; To Suspense a/c ₹520.
A sale to Uday Traders should have been a debit of ₹260 to their account. By wrongly crediting it, the account is now incorrect by double the amount (the missing ₹260 debit plus the wrong ₹260 credit). To rectify, Uday Traders' account must be debited with ₹520. The corresponding credit is posted to the Suspense account.

May/June 2021

61. After posting all the rectification entries from Illustration No. 5, what is the final balance of the Suspense Account?
(A) ₹771 Debit
(B) ₹771 Credit
(C) Zero
(D) ₹763 Debit

Ans :

(C) Zero
The Suspense Account began with a debit balance of ₹763. Rectification for the short credit to a creditor required a debit of ₹8. Rectification for the sales return undercasting required a credit of ₹251, and for the Uday Traders error a credit of ₹520. The total debits (₹763 + ₹8 = ₹771) now equal the total credits (₹251 + ₹520 = ₹771), so the account is closed with a zero balance.

Oct/Nov 2010

62. In Illustration No. 6, the trial balance credit side exceeded the debit side by ₹250. How is this initially recorded in the suspense account?
(A) As a credit balance of ₹250.
(B) As a debit balance of ₹250.
(C) As a debit to Profit & Loss Adjustment account for ₹250.
(D) As a credit to the Capital account for ₹250.

Ans :

(B) As a debit balance of ₹250.
If the credit side of the trial balance is greater than the debit side, it means the debit side is short. To make the totals agree, a debit amount equal to the difference must be introduced. This difference is placed on the debit side of the suspense account. Therefore, the suspense account will have an opening debit balance of ₹250.

May/June 2005

63. Goods of ₹620 sold to Long & Co. were correctly entered in the sales book but posted to their account as ₹260. What is the rectification entry?
(A) Suspense a/c Dr. ₹360; To Long & Co. a/c ₹360.
(B) Long & Co. a/c Dr. ₹620; To Suspense a/c ₹620.
(C) Long & Co. a/c Dr. ₹360; To Suspense a/c ₹360.
(D) Sales a/c Dr. ₹360; To Long & Co. a/c ₹360.

Ans :

(C) Long & Co. a/c Dr. ₹360; To Suspense a/c ₹360.
Long & Co.'s account (a debtor) should have been debited with ₹620 but was only debited with ₹260. This is a short debit of ₹360 (₹620 - ₹260).

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To correct this one-sided posting error, Long & Co.'s account must be debited by the difference of ₹360. The corresponding credit is made to the Suspense account.

Oct/Nov 2022

64. Goods of ₹75 sold to Short & Co. for cash were correctly entered in the cashbook, but wrongly credited to Short & Co.'s account. What is the rectification entry?

(A) Cash Sales a/c Dr. ₹75; To Short & Co. a/c ₹75.
(B) Short & Co. a/c Dr. ₹75; To Suspense a/c ₹75.
(C) Suspense a/c Dr. ₹75; To Cash Sales a/c ₹75.
(D) Short & Co. a/c Dr. ₹75; To Cash Sales a/c ₹75.

Ans :

(D) Short & Co. a/c Dr. ₹75; To Cash Sales a/c ₹75.
For a cash sale, the credit should be to the Sales account, not a personal account. Here, Short & Co. was wrongly credited instead of the Cash Sales account. To rectify, the wrong credit to Short & Co. must be reversed by debiting their account. The Cash Sales account must be credited to record the sale correctly.

May/June 2018

65. The total of the return outward book, ₹200, was not posted to the ledger. This is a partial omission. What is the rectification entry?

(A) Suspense a/c Dr. ₹200; To Return Outward a/c ₹200.
(B) Return Outward a/c Dr. ₹200; To Suspense a/c ₹200.
(C) Creditors a/c Dr. ₹200; To Return Outward a/c ₹200.
(D) Suspense a/c Dr. ₹200; To Creditors a/c ₹200.

Ans :

(A) Suspense a/c Dr. ₹200; To Return Outward a/c ₹200.
The Return Outward account normally has a credit balance. Failing to post the total means the credit side of the trial balance is short by ₹200. To rectify this one-sided error, the Return Outward account must be credited by ₹200. The corresponding debit entry is made to the Suspense account to complete the journal entry.

Oct/Nov 2016

66. Goods worth ₹100 were purchased from Broad & Co. but were entered in the sales book. The account of Broad & Co. was correctly credited. What is the rectification entry?

(A) Purchase a/c Dr. ₹100; To Sales a/c ₹100.
(B) Sales a/c Dr. ₹100; Purchase a/c Dr. ₹100; To Suspense a/c ₹200.
(C) Suspense a/c Dr. ₹200; To Sales a/c ₹100; To Purchase a/c ₹100.
(D) Sales a/c Dr. ₹100; To Suspense a/c ₹100.

Ans :

(B) Sales a/c Dr. ₹100; Purchase a/c Dr. ₹100; To Suspense a/c ₹200.
The error created a wrong credit to Sales (₹100) and omitted the correct debit to Purchases (₹100). Broad & Co.'s credit is correct. To rectify: (1) Debit Sales a/c for ₹100 to cancel the wrong credit. (2) Debit Purchase a/c for ₹100 to record the purchase. Both these debits total ₹200, which is balanced by crediting the Suspense account.

May/June 2014

67. A credit balance of a supplier's account of ₹110 was not carried forward. Based on the rectification shown in the Suspense Account T-account in the solution, what is the journal entry passed?

(A) Creditor a/c Dr. ₹110; To Suspense a/c ₹110.
(B) Suspense a/c Dr. ₹100; To Creditor a/c ₹100.
(C) Creditor a/c Dr. ₹110; To Sales a/c ₹110.
(D) Suspense a/c Dr. ₹110; To Creditor a/c ₹110.

Ans :

(D) Suspense a/c Dr. ₹110; To Creditor a/c ₹110.
Omitting a credit balance of ₹110 makes the credit side of the trial balance short. To rectify this, the creditor's account must be credited by ₹110. The corresponding debit is made to the suspense account. The T-account ledger for Suspense a/c shows an entry 'To Creditors 110' on the debit side, confirming this rectification entry.

Oct/Nov 2007

68. What happens to nominal accounts (expenses and incomes) at the end of an accounting year?

(A) They are closed by transferring their balances to the trading and profit and loss account.
(B) Their balances are carried forward to the balance sheet of the next year.
(C) They are temporarily transferred to the suspense account.
(D) They are shown as either assets or liabilities in the balance sheet.

Ans :

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(A) They are closed by transferring their balances to the trading and profit and loss account.
Nominal accounts measure financial performance for a specific period. At the end of the year, their purpose is fulfilled. They are closed by transferring their balances to the Trading and Profit and Loss Account to calculate the net profit or loss. This process resets their balances to zero for the start of the next accounting period.

May/June 2025

69. According to the section "Rectification of Errors when Books are Closed," why can't errors in nominal accounts discovered in the next year be adjusted to the current year's nominal accounts?
(A) Because it would require reopening the entire ledger from the previous year.
(B) Because all nominal accounts have a zero balance at the start of the new year.
(C) Because it will incorrectly affect the current year's profit and loss calculation.
(D) Because personal and real accounts are the only ones that can be adjusted.

Ans :

(C) Because it will incorrectly affect the current year's profit and loss calculation.
The text states that rectifying a prior-period error through a current-period nominal account would distort the current year's financial results. For example, correcting a missed expense from last year by debiting a current expense account would understate the current year's profit. To avoid this, a special account is used for such rectifications.

Oct/Nov 2019

70. When an error related to a nominal account is detected after the final accounts of a year are prepared, which new account is opened to rectify it?
(A) Profit and Loss Adjustment account
(B) Suspense Account
(C) Capital Account
(D) Prior Period Adjustment Account

Ans :

(A) Profit and Loss Adjustment account
Errors in nominal accounts from a previous, closed accounting period cannot be corrected through the current period's nominal accounts as this would distort current profits. Instead, a special temporary account called the 'Profit and Loss Adjustment account' is opened to handle these rectifications. The final balance of this adjustment account is then transferred directly to the Capital account.

May/June 2009

71. What is the ultimate disposition of the balance in the 'Profit and Loss Adjustment account'?
(A) It is carried forward to the next year's Balance Sheet as an asset or liability.
(B) It is transferred to the Suspense account to close it.
(C) It is shown as a separate item in the current year's Profit and Loss account.
(D) It is directly transferred to the capital account.

Ans :

(D) It is directly transferred to the capital account.
The Profit and Loss Adjustment account is used to ring-fence the profit impact of prior-period errors. Once all such errors are rectified through this account, its net debit or credit balance represents the total effect on the previous year's profit. This net balance is then transferred directly to the Capital account, correcting the owner's equity.

Oct/Nov 2011

72. Consider the error: Cash ₹350 received from Triman Chemicals was posted as ₹530 to their account. How would this be rectified before preparation of the trial balance?
(A) Pass an entry: Triman Chemicals a/c Dr. ₹180, To Suspense a/c ₹180.
(B) No journal entry is passed; Triman Chemicals account is simply debited with ₹180.
(C) Pass an entry: Suspense a/c Dr. ₹180, To Triman Chemicals a/c ₹180.
(D) No journal entry is passed; Triman Chemicals account is simply credited with ₹180.

Ans :

(B) No journal entry is passed; Triman Chemicals account is simply debited with ₹180.
The account was over-credited by ₹180 (₹530 - ₹350). Since this is a one-sided error detected before the trial balance is prepared, no formal journal entry is required. The correction is made by simply making a debit posting of ₹180 in the Triman Chemicals ledger account to reverse the excess credit.

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May/June 2010

73. Consider the error: Cash ₹350 received from Triman Chemicals was posted as ₹530 to their account. How would this be rectified after preparation of the trial balance but before final accounts?

(A) Debit Triman Chemicals a/c with ₹180.

(B) Suspense a/c Dr. ₹180; To Triman Chemicals a/c ₹180.

(C) Triman Chemicals a/c Dr. ₹180; To Suspense a/c ₹180.

(D) Triman Chemicals a/c Dr. ₹180; To P&L Adjustment a/c ₹180.

Ans :

(C) Triman Chemicals a/c Dr. ₹180; To Suspense a/c ₹180.

After a trial balance is prepared, one-sided errors are rectified using the Suspense account. Triman Chemicals' account was over-credited by ₹180. To correct this, their account must be debited with ₹180. The corresponding credit is made to the Suspense Account, which would have held the unexplained credit difference arising from this error.

Oct/Nov 2024

74. Consider the error: Cash ₹350 received from Triman Chemicals was posted as ₹530 to their account. How would this be rectified after preparing final accounts?

(A) Triman Chemicals a/c Dr. ₹180; To P&L Adjustment a/c ₹180.

(B) P&L Adjustment a/c Dr. ₹180; To Triman Chemicals a/c ₹180.

(C) Triman Chemicals a/c Dr. ₹180; To Capital a/c ₹180.

(D) Triman Chemicals a/c Dr. ₹180; To Suspense a/c ₹180.

Ans :

(D) Triman Chemicals a/c Dr. ₹180; To Suspense a/c ₹180.

Triman Chemicals is a personal account. The balances of personal and real accounts are carried forward from one year to the next. Therefore, even if the error is found after final accounts, the correction is made in the personal account itself. The P&L Adjustment account is only used for nominal accounts. The offset is to Suspense.

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May/June 2017

75. A payment of ₹260 for new office furniture was charged to office expenses. Based on the comparative table in Illustration 7, what is the rectification entry if the error is found after preparing final accounts?

(A) Office Furniture a/c Dr. ₹260; To Profit & Loss Adj. a/c ₹260.

(B) Office Furniture a/c Dr. ₹260; To Office Expenses a/c ₹260.

(C) Office Furniture a/c Dr. ₹260; To Suspense a/c ₹260.

(D) Profit & Loss Adj. a/c Dr. ₹260; To Office Furniture a/c ₹260.

Ans :

(A) Office Furniture a/c Dr. ₹260; To Profit & Loss Adj. a/c ₹260.

The error was debiting a nominal account (Office Expenses) instead of a real account (Office Furniture). When found after final accounts, the nominal account is already closed. Therefore, the correction must use the Profit & Loss Adjustment account. The entry is to debit Office Furniture to record the asset and credit the P&L Adjustment account to reverse the prior year's expense.

Oct/Nov 2005

76. Purchase of stationery for ₹150 remained unposted from the cashbook. What is the rectification entry if this is found after the trial balance is prepared but before final accounts?

(A) Stationery a/c Dr. ₹150; To Cash a/c ₹150.

(B) Stationery a/c Dr. ₹150; To Suspense a/c ₹150.

(C) Suspense a/c Dr. ₹150; To Stationery a/c ₹150.

(D) Profit & Loss Adj. a/c Dr. ₹150; To Suspense a/c ₹150.

Ans :

(B) Stationery a/c Dr. ₹150; To Suspense a/c ₹150.

This is a one-sided error; the credit to cash was made, but the debit to stationery was missed. When found after the trial balance, the missing debit to the Stationery account must be made. The corresponding credit is posted to the Suspense account, which would be holding the unexplained difference caused by this omission.

May/June 2020

77. Purchase of stationery worth ₹150 remained unposted from the cashbook. How is this rectified if found after preparing final accounts?
(A) Stationery a/c Dr. ₹150; To Suspense a/c ₹150.
(B) Stationery a/c Dr. ₹150; To P&L Adj. a/c ₹150.
(C) Profit & Loss Adj. a/c Dr. ₹150; To Cash a/c ₹150.
(D) Profit & Loss Adj. a/c Dr. ₹150; To Suspense a/c ₹150.

Ans :

(D) Profit & Loss Adj. a/c Dr. ₹150; To Suspense a/c ₹150.
The Stationery account is a nominal account, which would have been closed at the end of the previous year. Therefore, the rectification cannot be made to the Stationery account directly. Instead, the Profit & Loss Adjustment account is debited. The corresponding credit is made to the Suspense account to correct the one-sided error.

Oct/Nov 2015

78. A credit sale of ₹400 to Trivedi & Co. was posted to the credit of their account. If found before the trial balance, what is the rectification?
(A) Debit Trivedi & Co. with ₹800.
(B) Credit Trivedi & Co. with ₹800.
(C) Pass entry: Trivedi & Co. Dr. ₹800; To Suspense a/c ₹800.
(D) Pass entry: Suspense a/c Dr. ₹800; To Trivedi & Co. a/c ₹800.

Ans :

(A) Debit Trivedi & Co. with ₹800.
A credit sale should be debited to the customer's account. Posting it as a credit makes the account wrong by double the amount. The required correction is a debit of ₹800 (to cancel the ₹400 wrong credit and establish the correct ₹400 debit). As it's a one-sided error found before the trial balance, a simple posting is made without a journal entry.

May/June 2013

79. A credit sale of ₹400 to Trivedi & Co. was posted to the credit of their account. If this error is found after preparing final accounts, what is the rectification entry?
(A) Trivedi & Co. a/c Dr. ₹800; To P&L Adjustment a/c ₹800.
(B) Trivedi & Co. a/c Dr. ₹400; To Suspense a/c ₹400.
(C) Trivedi & Co. a/c Dr. ₹800; To Suspense a/c ₹800.
(D) Suspense a/c Dr. ₹800; To Trivedi & Co. a/c ₹800.

Ans :

(C) Trivedi & Co. a/c Dr. ₹800; To Suspense a/c ₹800.
The rectification requires a debit of ₹800 to Trivedi & Co.'s account. Since Trivedi & Co. is a personal account, its balance is carried forward, so the correction can be made directly to it. As it's a one-sided error, the corresponding credit is posted to the Suspense account, regardless of whether it's found before or after final accounts.

Oct/Nov 2021

80. What is the primary purpose of passing 'Adjusting Entries'?
(A) To account for expenses incurred but not paid, and income due but not received.
(B) To correct clerical errors and errors of principle made during the year.
(C) To close all nominal accounts at the end of the accounting period.
(D) To transfer the trial balance difference to a temporary suspense account.

Ans :

(A) To account for expenses incurred but not paid, and income due but not received.
Adjusting entries are made at the end of an accounting period to ensure that the financial statements reflect all revenues earned and all expenses incurred during that period, regardless of when cash was exchanged. This adheres to the accrual basis of accounting and helps in presenting a true and fair view of the business's performance and position.

May/June 2024

81. Entries passed to transfer the balances of all expense and income accounts to the trading and profit and loss account are known as:
(A) Adjusting Entries
(B) Rectifying Entries
(C) Closing Entries
(D) Opening Entries

Ans :

(C) Closing Entries

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At the end of the accounting year, all nominal accounts (incomes and expenses) must be reset to zero to begin the next period. This is achieved by passing 'Closing Entries', which transfer the balances from these individual revenue and expense accounts into the Trading and Profit and Loss account, where the net profit or loss is ultimately calculated.

Oct/Nov 2008

82. Which of the following statements is a correct summary of rectifying one-sided errors?

(A) They are always rectified using the suspense account, regardless of timing.

(B) If located after the trial balance is prepared, rectification involves the suspense account.

(C) If located before the trial balance, a formal journal entry is always passed.

(D) They always involve the Profit & Loss Adjustment account if found in a subsequent year.

Ans :

(B) If located after the trial balance is prepared, rectification involves the suspense account.

The method for rectifying a one-sided error depends on when it is found. If discovered before the trial balance is prepared, a simple corrective posting suffices. However, if it is located after the trial balance has been prepared and a difference placed in suspense, a formal journal entry must be passed using the suspense account as the offset.

May/June 2006

83. Match List-I (Type of Error) with List-II (Example).

List-I

P. Error of Principle

Q. Error of Commission

R. Error of Omission

S. Compensating Error

List-II

1. Credit sale to Ram not recorded in the books.
2. Purchase of furniture debited to Purchases account.
3. Sales account overcast by ₹100, and Rent account undercast by ₹100.
4. Sale of ₹550 to Suresh posted to his account as ₹505.

(A) P-2, Q-4, R-1, S-3

(B) P-1, Q-2, R-3, S-4

(C) P-2, Q-1, R-4, S-3

(D) P-3, Q-4, R-1, S-2

Ans :

(A) P-2, Q-4, R-1, S-3

P (Principle) matches 2 (treating capital as revenue). Q (Commission) matches 4 (posting wrong amount). R (Omission) matches 1 (complete omission of a transaction). S (Compensating) matches 3 (one error's effect is cancelled by another). This correctly pairs each error type with its corresponding example, reflecting the definitions provided in the chapter.

Oct/Nov 2017

84. Which of the following errors will be revealed by a trial balance?

(A) Purchase of a computer for ₹30,000 debited to office expenses.

(B) A credit purchase of ₹5,000 was not recorded in the purchase book.

(C) Goods sold to a customer for ₹1,000 were correctly recorded in the sales book but omitted from posting to the customer's account.

(D) A payment of ₹2,500 for salaries was posted twice as a complete journal entry.

Ans :

(C) Goods sold to a customer for ₹1,000 were correctly recorded in the sales book but omitted from posting to the customer's account.

This is a partial omission error. The sales account is credited when the sales book is totaled, but the corresponding debit to the customer's account is missed. This creates an imbalance where the credit side of the trial balance is higher than the debit side, thus causing the trial balance to disagree and reveal the error.

May/June 2008

85. Which of the following errors will NOT affect the agreement of a trial balance?

(A) Wrongly debiting a personal account instead of an expense account.

(B) Posting a correct amount to the wrong side of a ledger account.

(C) A totaling error in the purchase journal not yet posted.

(D) Omitting to post the credit entry of a transaction while the debit entry is posted.

Ans :

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(A) Wrongly debiting a personal account instead of an expense account.
This is an error of principle. Although the wrong type of account is used (personal instead of nominal), a debit is still recorded correctly, and the corresponding credit is also recorded. The fundamental rule of double-entry is followed, maintaining the equality of total debits and credits. Therefore, the trial balance will still agree despite this error.

Oct/Nov 2013

86. Statement (I): A Net Trial Balance shows the total of the debit and credit sides for each ledger account. Statement (II): A Gross Trial Balance shows only the final debit or credit balance for each ledger account.
(A) Both statements are correct.
(B) Both statements are incorrect.
(C) Statement (I) is correct, but Statement (II) is incorrect.
(D) Statement (I) is incorrect, but Statement (II) is correct.

Ans :

(B) Both statements are incorrect.
Both statements have reversed the definitions. A Gross Trial Balance is the one that shows the total of the debit and credit sides for each account. A Net Trial Balance is the one that is more commonly used and shows only the final net debit or credit balance for each account. Therefore, both statements are factually incorrect.

May/June 2015

87. **Assertion (A) :** An error of principle does not cause the trial balance to disagree.
Reason (R) : In an error of principle, the transaction is recorded by following the rules of debit and credit, although in the wrong class of account.
(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
Assertion (A) is true; errors of principle do not affect trial balance agreement. Reason (R) is also true and correctly explains why. For example, debiting an expense instead of an asset still involves a correct debit amount against a correct credit amount, maintaining the debit-credit equality. The error is in classification, not arithmetic, which is why the trial balance agrees.

Oct/Nov 2012

88. **Assertion (A) :** Posting a debit of ₹500 as a credit of ₹500 will cause the trial balance to be out by ₹1,000.
Reason (R) : When an amount is posted to the wrong side of an account, the difference will be double the amount.
(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
The assertion is correct; the trial balance will be out of balance by ₹1,000. The reason correctly explains this phenomenon. The intended debit of ₹500 is missing, making the debit side short by ₹500. A wrong credit of ₹500 is added, making the credit side excess by ₹500. The total difference is ₹500 + ₹500 = ₹1,000.

May/June 2011

89. A trial balance showed an excess debit of ₹500, which was placed in a suspense account (credit balance). Later, it was found that a cash receipt of ₹250 from a customer was wrongly debited to his account. What is the rectification entry?
(A) Customer a/c Dr. ₹250; Suspense a/c Cr. ₹250
(B) Customer a/c Cr. ₹250; Suspense a/c Dr. ₹250
(C) Customer a/c Cr. ₹500; Suspense a/c Dr. ₹500
(D) Suspense a/c Cr. ₹500; Customer a/c Dr. ₹500

Ans :

(C) Customer a/c Cr. ₹500; Suspense a/c Dr. ₹500
A cash receipt should be credited to the customer's account. Wrongly debiting it for ₹250 means the account is incorrect by double the amount (₹500). To rectify, the customer's account must be credited by ₹500. This correction explains the entire difference in the trial balance, so the corresponding debit of ₹500 is made to the suspense account, closing it.

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Oct/Nov 2020

90. Identify the correct statement(s) regarding a Trial Balance.

1. It is a part of the double-entry system.
2. It provides conclusive proof of the accuracy of accounts.
3. It is a list of balances of all ledger accounts, including cash and bank.

(A) Only 3
(B) 1 and 3
(C) 2 and 3
(D) All 1, 2, and 3

Ans :

(A) Only 3
Statement 3 is the correct definition. Statement 1 is incorrect; a trial balance is a statement prepared from the results of the double-entry system, but it is not an account or a book within the system itself. Statement 2 is incorrect because a trial balance only proves arithmetical accuracy and can still agree despite errors of omission or principle.

May/June 2022

91. Which of the following errors would cause a difference in the trial balance?

1. An amount of ₹1,000 received from a debtor is not recorded in the cash book.
2. Sales day book is overcast by ₹5,000.
3. Purchase of office equipment of ₹10,000 is recorded in the purchases day book.
4. Wages paid to a worker ₹2,000 is debited to his personal account.

(A) 2 and 4
(B) 1 and 3
(C) Only 4
(D) Only 2

Ans :

(D) Only 2
Overcasting the sales day book (2) is a one-sided error in totaling that will cause the credit side of the trial balance to be higher. Error (1) is a complete omission. Errors (3) and (4) are errors of principle. Errors of complete omission and principle do not cause the trial balance to disagree.

Oct/Nov 2023

92. Consider the following statements:
Statement I : Rectifying entries for errors detected after the preparation of final accounts for nominal accounts are passed through the Profit and Loss Adjustment Account.
Statement II : The balance of the Profit and Loss Adjustment Account is ultimately transferred to the Suspense Account.

(A) Statement I is correct, but Statement II is incorrect.
(B) Statement I is incorrect, but Statement II is correct.
(C) Both statements are correct.
(D) Both statements are incorrect.

Ans :

(A) Statement I is correct, but Statement II is incorrect.
Statement I is correct. To avoid distorting the current year's profit, prior-period errors in nominal accounts are rectified via the P&L Adjustment Account. Statement II is incorrect. The final balance of the P&L Adjustment Account is transferred directly to the Capital Account to correct the owner's equity, not to the Suspense Account.

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May/June 2016

93. What is the correct sequence of steps in preparing a Net Trial Balance?

1. List the names of all ledger accounts.
2. Calculate the net balance of each ledger account.
3. Place the net debit balances in the debit column and net credit balances in the credit column.
4. Total the debit and credit columns.

(A) 1, 2, 4, 3
(B) 1, 3, 2, 4
(C) 2, 1, 3, 4
(D) 2, 3, 1, 4

Ans :

(C) 2, 1, 3, 4
The logical process begins with the ledger accounts. First, you must calculate the net balance (debit or credit) for each account (2). Then, you create the statement by listing the account names (1), entering their respective balances in the correct debit or credit column (3), and finally, summing the columns to verify they are equal (4).

Oct/Nov 2009

94. Identify the incorrect pair.
(A) Error of Principle : Does not affect Trial

Balance agreement.
(B) Partial Omission : Affects Trial Balance agreement.
(C) Error of Commission : Can affect Trial Balance agreement.
(D) Compensating Error : Affects Trial Balance agreement.

Ans :

(D) Compensating Error : Affects Trial Balance agreement.
A compensating error is one where two or more mistakes cancel each other out. For example, an overcast of ₹100 in one account is offset by an undercast of ₹100 in another. Because the errors nullify each other's effect on the totals, the trial balance agreement is not affected. Therefore, this pairing is incorrect.

May/June 2023

95. A trial balance can be prepared:
(A) At any time as and when required.
(B) Only on a monthly basis for internal control.
(C) Only on a quarterly basis for reporting.
(D) Only at the end of the financial year for statutory purposes.

Ans :

(A) At any time as and when required.
While commonly prepared at year-end before creating final accounts, a trial balance is a versatile tool for checking arithmetical accuracy. It can be generated at any frequency desired by the management, such as monthly, quarterly, or half-yearly, to ensure the books are being maintained correctly throughout the accounting period and to facilitate interim reporting.

Oct/Nov 2018

96. Match List-I (Account Type from Illus. 2) with List-II (Trial Balance Column).
List-I
P. Bank Overdraft
Q. Loan to Y
R. Discount earned
S. Machinery
List-II
1. Debit
2. Credit
(A) P-2, Q-1, R-2, S-1
(B) P-1, Q-2, R-1, S-2
(C) P-2, Q-1, R-1, S-2
(D) P-1, Q-2, R-2, S-1

Ans :

(A) P-2, Q-1, R-2, S-1
Bank Overdraft (P) is a liability, so it's a credit (2). Loan to Y (Q) is an asset (money lent out), so it's a debit (1). Discount earned (R) is an income, so it's a credit (2). Machinery (S) is an asset, so it's a debit (1). The correct matching is therefore P-2, Q-1, R-2, S-1.

May/June 2007

97. Which of the following is NOT an example of an Error of Commission?
(A) Posting of a correct amount but on the wrong side of an account.
(B) Posting of a wrong amount but on the correct side of an account.
(C) An incorrect totaling (casting) error in a subsidiary book.
(D) A credit purchase of goods not recorded in the purchase journal.

Ans :

(D) A credit purchase of goods not recorded in the purchase journal.
This is an example of a complete 'Error of Omission', where the transaction is entirely left out of the books. Errors of commission involve mistakes made during the act of recording or posting, such as using the wrong amount, wrong side, or wrong account, or making a totaling error. Omitting the entry altogether is a different category of error.

Oct/Nov 2025

98. An amount of ₹800 paid for freight on machinery was debited to the Freight account. The rectification entry involves:
(A) Debiting Machinery a/c and crediting Freight a/c.
(B) Debiting Freight a/c and crediting Machinery a/c.
(C) Debiting Machinery a/c and crediting Suspense a/c.
(D) Debiting P&L Adjustment a/c and crediting Freight a/c.

Ans :

(A) Debiting Machinery a/c and crediting Freight a/c.
This is an error of principle. Freight on the purchase of machinery is a capital expenditure and should be added to the cost of the

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machinery. By debiting the Freight account (a revenue expense), the error understated assets and overstated expenses. To rectify, debit the Machinery account and credit the Freight account to reverse the incorrect entry.

May/June 2012

99. If a suspense account does not balance after all known errors are rectified, the remaining balance is:
(A) Transferred to the Profit & Loss account for the current period.
(B) Transferred directly to the Capital account as a correction of equity.
(C) Carried forward in the Balance Sheet.
(D) Written off as a miscellaneous expense or income.

Ans :

(C) Carried forward in the Balance Sheet.
If a balance remains in the suspense account after all rectification efforts, it signifies an as-yet-undiscovered error. This balance cannot be written off. It is carried forward to the Balance Sheet pending investigation. A debit balance is shown on the asset side, and a credit balance is shown on the liability side.

Oct/Nov 2014

100. From the Net Trial Balance of Mr. Bhagwandas, which of the following accounts has a credit balance?
(A) Suppliers
(B) Drawings
(C) Customers
(D) Car

Ans :

(A) Suppliers
In the Net Trial Balance, Suppliers (creditors) represent a liability, which is the amount owed by the business. Liabilities always have a credit balance. Drawings, Customers (debtors), and Car (asset) are all accounts that typically have debit balances. The solved Net Trial Balance for Mr. Bhagwandas confirms a credit balance of ₹35,000 for Suppliers.

May/June 2019

101. Which of the following is considered a two-sided error?
(A) The total of the sales book was carried forward as ₹1,200 instead of ₹1,000.
(B) A payment of ₹500 to a creditor was not posted to his account from the cash book.
(C) The balance of the cash book was not brought forward in the ledger.
(D) A purchase of goods from Mr. X for ₹2,000 was entered in the sales book.

Ans :

(D) A purchase of goods from Mr. X for ₹2,000 was entered in the sales book.
This error affects multiple accounts incorrectly. It wrongly credits the Sales account and wrongly debits a debtor's account, while also omitting the correct debit to the Purchases account and the correct credit to Mr. X's account. This involves multiple incorrect debits and credits, making it a two-sided error requiring a comprehensive rectification entry.

Oct/Nov 2006

102. 'Adjusting Entries' are passed based on which accounting concept?
(A) Business Entity Concept
(B) Accrual Concept
(C) Money Measurement Concept
(D) Dual Aspect Concept

Ans :

(B) Accrual Concept
The Accrual Concept dictates that revenues and expenses should be recognized when they are earned or incurred, not necessarily when cash is received or paid. Adjusting entries for items like outstanding expenses, prepaid expenses, accrued income, and income received in advance are passed specifically to comply with this fundamental accounting concept.

May/June 2021

103. If salary paid is ₹5,000, but the amount debited to the salary account is only ₹500, which error is this?
(A) Error of principle
(B) Error of omission
(C) Error of commission
(D) Compensating error

Ans :

(C) Error of commission
This is a classic 'Error of Commission', specifically, posting a wrong amount. The transaction was recorded, and the correct account was used, but a mistake was made in the numerical value

NODIA

entered. This type of clerical mistake will cause the trial balance to disagree, as the debit to salary will not match the credit to cash/bank.

Oct/Nov 2010

104. Which of the following steps is taken if the trial balance disagrees and the difference is suspected to be due to a transposition error?
(A) The difference amount is halved to check for wrong-side postings.
(B) The difference amount is doubled to check for reversal entries.
(C) All ledger account balances are re-checked from the beginning.
(D) The difference amount is checked to see if it is divisible by 9.

Ans :

(D) The difference amount is checked to see if it is divisible by 9.
A transposition error is when two digits in a number are accidentally swapped (e.g., writing 72 as 27). A mathematical property of such errors is that the difference between the original number and the transposed number is always divisible by 9 (e.g., 72 - 27 = 45, which is divisible by 9). This provides a quick diagnostic test.

May/June 2005

105. Statement (I): A trial balance is an account. Statement (II): A trial balance is prepared to check the arithmetical accuracy of the ledger accounts.
(A) Both (I) and (II) are correct.
(B) (I) is correct, but (II) is incorrect.
(C) (I) is incorrect, but (II) is correct.
(D) Both (I) and (II) are incorrect.

Ans :

(C) (I) is incorrect, but (II) is correct.
Statement (I) is incorrect; a trial balance is a statement or a list, not an account, as it does not have debit and credit sides in the T-account format. Statement (II) is correct; the primary purpose of preparing a trial balance is to verify that the total debits equal the total credits in the ledger, ensuring arithmetical accuracy.

Oct/Nov 2022

106. The process of transferring the balances from the nominal accounts to the Trading and P&L account is called:
(A) Balancing
(B) Closing
(C) Adjusting
(D) Rectifying

Ans :

(B) Closing
At the end of an accounting period, nominal accounts (revenues and expenses) have served their purpose of tracking performance for that period. The 'closing' process involves passing journal entries to transfer their balances to the Trading and Profit & Loss account, effectively resetting them to zero for the next period and facilitating profit calculation.

May/June 2018

107. If a credit balance of ₹700 in a supplier's account is mistakenly shown as a debit balance in the trial balance, the trial balance will be out of agreement by:
(A) ₹700 (Debit side higher)
(B) ₹700 (Credit side higher)
(C) ₹1,400 (Credit side higher)
(D) ₹1,400 (Debit side higher)

Ans :

(D) ₹1,400 (Debit side higher)
This error has a dual effect. The credit side is missing the correct credit of ₹700, and the debit side is inflated by an incorrect debit of ₹700. The total discrepancy between the two sides is the sum of these two impacts, resulting in the debit side being higher than the credit side by ₹1,400.

Oct/Nov 2016

108. An entry of ₹1,200 was correctly recorded in the Sales Journal, but while posting to the debtor's account, it was posted as ₹120. This is an:
(A) Error of commission.
(B) Error of principle.
(C) Error of complete omission.
(D) Error of partial omission.

Ans :

(A) Error of commission.
This mistake is classified as an error of commission because an entry was made in the correct account and on the correct side, but with the wrong amount. The sales journal entry was correct, but the posting to the subsidiary ledger account was incorrect. This clerical error in posting will cause the trial balance to disagree.

NODIA

May/June 2014

109. Which of the following errors would not be disclosed by a trial balance?
(A) Sales of ₹500 were recorded as ₹50 in the sales book.
(B) Sales of ₹500 were posted as ₹50 to the customer's account.
(C) Sales of ₹500 were not recorded in the sales book.
(D) Sales of ₹500 were credited to the customer's account.

Ans :

(C) Sales of ₹500 were not recorded in the sales book.
This is an error of complete omission. Since neither the debit aspect (to the customer) nor the credit aspect (to sales) of the transaction was recorded, the fundamental equality of debits and credits is maintained. The trial balance will therefore agree, but the accounts are incomplete and inaccurate, hiding this error from detection via balancing.

Oct/Nov 2007

110. The suspense account is a:
(A) Temporary Account
(B) Real Account
(C) Personal Account
(D) Nominal Account

Ans :

(A) Temporary Account
A suspense account is not a standard real, personal, or nominal account. It is a temporary holding account created for the specific purpose of making the trial balance agree when there is a difference. It is expected to be cleared and have a zero balance once the underlying errors have been located and rectified.

May/June 2025

111. Identify the correct statement regarding rectification of errors.
(A) One-sided errors are always rectified by passing a journal entry with suspense.
(B) Errors of principle do not require rectification as the trial balance agrees.
(C) The Suspense account is used to rectify all types of accounting errors.
(D) Two-sided errors are rectified by passing a journal entry affecting two or more accounts.

Ans :

(D) Two-sided errors are rectified by passing a journal entry affecting two or more accounts.
Two-sided errors, by definition, involve incorrect entries in at least two accounts. To correct such errors, a formal rectification journal entry is necessary to properly adjust the debit and credit in all affected accounts. One-sided errors may not require a journal entry if found before the trial balance is prepared.

Oct/Nov 2019

112. A firm's trial balance has a difference of ₹360 (excess credit). This could be due to:
(A) A purchase of ₹360 not posted from the purchase book to the creditor's ledger.
(B) A sale of ₹360 not posted from the sales book to the debtor's ledger.
(C) A payment of ₹180 to a creditor being wrongly debited to his account instead of credited.
(D) A receipt of ₹180 from a debtor being wrongly credited to his account twice.

Ans :

(B) A sale of ₹360 not posted from the sales book to the debtor's ledger.
An excess credit of ₹360 means the debit side is short by ₹360. A sale not posted to the debtor's ledger means the required debit of ₹360 to the debtor's account was missed. The credit to sales was correctly made through the sales book total. This partial omission results in a short debit of ₹360, matching the difference.

May/June 2009

113. Consider the transactions for Mr. Inderkumar. The balance of 'Printing & Stationery' (₹6,000) will appear on which side of the trial balance?
(A) Credit side, as it is an income for the business.
(B) Credit side, as it is a liability owed by the business.
(C) Debit side, as it is an expense incurred by the business.
(D) Debit side, as it is considered a tangible asset.

Ans :

(C) Debit side, as it is an expense incurred by the business.
'Printing & Stationery' represents an operating cost incurred by the business. All expenses, according to the rules of accounting, have debit balances. Therefore, when preparing the trial

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balance for Mr. Inderkumar, the ₹6,000 balance for this account must be placed in the debit column along with other assets and expenses.

Oct/Nov 2011

114. The balance of 'Inderkumar's capital' (₹15,000) will be shown on which side of the trial balance?
(A) Debit side, as it is an investment in the business.
(B) Debit side, as it is similar to an asset of the business.
(C) Credit side, as it represents the total profit of the business.
(D) Credit side, as it is a liability of the business to the owner.

Ans :

(D) Credit side, as it is a liability of the business to the owner.
According to the business entity concept, the business is separate from its owner. The capital contributed by the owner is treated as an amount that the business owes to the owner. This 'internal liability' or owner's equity is represented by a credit balance in the trial balance.

May/June 2010

115. A trial balance is a statement containing the balances of:
(A) All ledger accounts.
(B) Only personal and real accounts.
(C) Only real and nominal accounts.
(D) Only personal and nominal accounts.

Ans :

(A) All ledger accounts.
A trial balance is a comprehensive summary prepared to check the arithmetical accuracy of the bookkeeping process. To be complete, it must include the balances of every single account maintained in the general ledger, which encompasses all personal, real, and nominal accounts, as well as cash and bank balances from the cash book.

Oct/Nov 2024

116. If the trial balance totals do not agree, the difference must be entered in:
(A) The Profit & Loss Account
(B) A Suspense Account
(C) The Capital Account
(D) The Balance Sheet directly

Ans :

(B) A Suspense Account
When the trial balance fails to agree, it indicates one or more errors. To proceed with preparing financial statements without delay, the difference between the debit and credit totals is temporarily placed in a Suspense Account. This allows the trial balance to be 'forced' into agreement while investigations to find the error(s) continue.

May/June 2017

117. An error in casting the sales day book would be an example of:
(A) An error of omission
(B) An error of principle
(C) An error of commission
(D) A compensating error

Ans :

(C) An error of commission
'Casting' refers to the process of totaling a column or a book. An error in this process, such as an incorrect addition of the sales day book, is a type of clerical mistake. It falls under the category of an error of commission, as it is a mistake made in the execution of an accounting procedure.

Oct/Nov 2005

118. Which of the following will cause the trial balance to be out of balance?
(A) A cash payment of ₹800 for rent was posted to the debit of the rent account as ₹80.
(B) An invoice for ₹1,450 was entered in the sales book and posted to the debtor as ₹1,540.
(C) A purchase of ₹2,000 from 'A' was entered in the ledger account of 'B'.
(D) A sale of old furniture was credited to the sales account instead of the furniture account.

Ans :

(A) A cash payment of ₹800 for rent was posted to the debit of the rent account as ₹80.
This is a one-sided error of commission. The credit to the cash account would be for the correct amount of ₹800, but the debit to the rent account is for the incorrect amount of ₹80. This discrepancy between the debit and credit postings for the same transaction will cause the trial balance totals to disagree.

May/June 2020

119. A 'Closing Entry' is one which:
(A) Is passed at the beginning of an accounting

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period to open the books.
(B) Corrects a clerical or principle error found in the books of account.
(C) Closes the nominal accounts by transferring them to the Trading and P&L account.
(D) Is passed to record outstanding expenses and accrued incomes.

Ans :

(C) Closes the nominal accounts by transferring them to the Trading and P&L account.
Closing entries are a crucial step in the accounting cycle performed at the end of the period. Their specific purpose is to transfer the balances of all temporary accounts (revenues, expenses, gains, and losses) to a permanent equity account (via the Trading and P&L account), thereby resetting their balances to zero for the next period.

Oct/Nov 2015

120. Rectification of errors detected before the preparation of the trial balance:
(A) Can be done by making corrective postings for one-sided errors without a journal entry.
(B) Requires passing formal journal entries for all types of errors.
(C) Involves using a suspense account for all one-sided errors.
(D) Is not possible; errors can only be rectified after the trial balance is prepared.

Ans :

(A) Can be done by making corrective postings for one-sided errors without a journal entry.
When one-sided errors are found before the trial balance is prepared, the ledger is still considered 'open'. The most efficient method of correction is to make a direct posting on the correct side of the affected account with an explanatory note. A formal journal entry and the use of a suspense account are not necessary at this stage.

May/June 2013

121. Based on the source, "An amount received from a customer Ramesh ₹2,000 recorded correctly in the cash book but posted to the debit side of Ramesh's account in the ledger," what type of error is this and what is its effect?
(A) Error of principle; trial balance agrees.
(B) Partial omission; trial balance disagrees.
(C) Error of commission; trial balance disagrees.
(D) Compensating error; trial balance agrees.

Ans :

(C) Error of commission; trial balance disagrees.
The error described is posting to the wrong side of an account, which is a classic error of commission. The cash book entry is correct (debit cash), but Ramesh's account was debited instead of credited. This doubles the error's impact on the debit side, causing the trial balance to disagree, as explicitly stated in the text.

Oct/Nov 2021

122. As per Illustration 7, a credit sale of ₹400 to Trivedi & Co. was posted to the credit of their account. This is a one-sided error. What is the value of the rectification entry required to correct Trivedi & Co.'s account?
(A) ₹200
(B) ₹800
(C) ₹400
(D) ₹600

Ans :

(B) ₹800
A credit sale should have been a debit of ₹400. Instead, a credit of ₹400 was posted. To correct this, the accountant must first cancel the wrong credit of ₹400 (by debiting ₹400) and then post the correct debit of ₹400. The total debit required in the rectification entry is therefore ₹400 + ₹400 = ₹800.

May/June 2024

123. The source states, "If expenses have been incurred but not paid or income is due but not received, necessary entries are required to be passed to show the correct picture of the business. These entries are called 'Adjusting Entries'." Which accounting principle does this practice uphold?
(A) Going Concern Principle
(B) Cost Principle
(C) Matching Principle and Accrual Basis
(D) Business Entity Principle

Ans :

(C) Matching Principle and Accrual Basis
The description directly relates to the accrual basis of accounting, where transactions are recorded when they occur, not when cash changes hands. This practice also upholds the matching principle, which requires that expenses incurred to generate revenue be recorded in the same period as that revenue, which is achieved

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through adjusting entries for accrued and outstanding items.

Oct/Nov 2008

124. In Illustration 6, a bookkeeper detected several errors after putting a difference of ₹250 (credit excess) into a suspense account. One error was the total of the return outward book (₹200) was not posted. How does rectifying this single error affect the suspense account?
(A) The suspense account is credited by ₹200.
(B) The suspense account is credited by ₹400.
(C) The suspense account is debited by ₹400.
(D) The suspense account is debited by ₹200.

Ans :

(D) The suspense account is debited by ₹200.
Return Outward has a credit balance. Failing to post it means the credit side of the trial balance was understated. The rectification entry is to debit the Suspense account and credit the Return Outward account. Therefore, the suspense account (which had an initial debit balance of ₹250) is further debited by ₹200.

May/June 2006

125. The source, "The Directory for Accountants, written by Eric. L. Kohler, defines Trial Balance as ... to establish a basic summary for financial statements," implies that a trial balance serves as a:
(A) Connecting link between ledger accounts and financial statements.
(B) Final financial statement itself, similar to a balance sheet.
(C) Complete substitute for the general ledger.
(D) Formal record of non-financial business transactions.

Ans :

(A) Connecting link between ledger accounts and financial statements.
The definition highlights that a trial balance is a "basic summary for financial statements." This indicates its role as an intermediate step. It summarizes all the balances from the ledger and organizes them in a way that facilitates the easy preparation of the Profit and Loss Account and the Balance Sheet.

Oct/Nov 2017

126. A credit purchase of ₹1,500 from Ravi was correctly recorded in the Purchases Book. However, Ravi's account was credited with ₹150. To rectify this, the rectification entry will be:
(A) Debit Ravi's a/c ₹1,350; Credit Suspense a/c ₹1,350
(B) Debit Suspense a/c ₹1,350; Credit Ravi's a/c ₹1,350
(C) Debit Purchases a/c ₹1,350; Credit Ravi's a/c ₹1,350
(D) Debit Ravi's a/c ₹1,350; Credit Purchases a/c ₹1,350

Ans :

(B) Debit Suspense a/c ₹1,350; Credit Ravi's a/c ₹1,350
Ravi's account was short-credited by ₹1,350 (₹1,500 - ₹150). This is a one-sided error. To correct it, Ravi's account must be credited by the shortfall of ₹1,350. Assuming this is found after the trial balance is prepared, the corresponding debit to complete the entry is made to the Suspense account.

May/June 2008

127. Which of the following statements is true?
(A) A trial balance is a book of prime entry like a journal.
(B) A trial balance will not tally if a transaction is completely omitted.
(C) A trial balance is prepared after preparing the financial statements.
(D) A trial balance verifies the arithmetical accuracy of the ledger.

Ans :

(D) A trial balance verifies the arithmetical accuracy of the ledger.
The fundamental purpose of a trial balance is to act as a check on the bookkeeping process. By confirming that the sum of all debit balances from the ledger equals the sum of all credit balances, it helps to verify the arithmetical accuracy of the postings made under the double-entry system.

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Oct/Nov 2013

128. An amount of ₹5,000 paid to a supplier was debited to the Purchases account. This is an:
(A) Error of Commission
(B) Error of Omission
(C) Error of Principle
(D) Compensating Error

Ans :

(A) Error of Commission

This is an error of commission, specifically posting to the wrong account. A payment to a supplier should be debited to the supplier's personal account to reduce the liability. Debiting the Purchases account is an incorrect posting. Since it involves an incorrect account, it falls under the classification of an error of commission.

May/June 2015

129. If the suspense account has a credit balance of ₹1,000, it means:

(A) The debit side of the trial balance was ₹1,000 more than the credit side.

(B) The credit side of the trial balance was ₹1,000 more than the debit side.

(C) An asset of ₹1,000 was omitted from the books.

(D) An expense of ₹1,000 was omitted from the books.

Ans :

(A) The debit side of the trial balance was ₹1,000 more than the credit side.

A suspense account is used to balance the trial balance. If the suspense account has a credit balance, it means a credit was needed to make the trial balance tally. This implies that before the suspense account was used, the debit side total was greater than the credit side total by that amount.

Oct/Nov 2012

130. The rectification of an error of principle:

(A) Will always affect two or more accounts.

(B) Will always involve the suspense account for correction.

(C) Will affect only one account in the ledger.

(D) Is not necessary if the trial balance agrees.

Ans :

(A) Will always affect two or more accounts.

An error of principle involves treating an item incorrectly, such as a capital expenditure as revenue. Rectifying this requires moving the amount from the wrong account to the right one (e.g., from Wages account to Machinery account). This correction will, by its nature, always involve passing a journal entry that affects at least two accounts.

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CHAPTER 6

Depreciation and Its Accounting

Oct/Nov 2014

1. According to the chapter's structure, which topic is discussed immediately before the 'Methods of Depreciation'?
   (A) Causes of Depreciation
   (B) Accounting Entries
   (C) Need for Depreciation
   (D) Factors of Depreciation

   Ans :

   (B) Accounting Entries
   The chapter structure lists the topics in a logical sequence. The section '6.5 Accounting Entries' is presented directly before '6.6 Methods of Depreciation'. This order ensures that the student first understands how depreciation is recorded in the books of accounts before learning about the different methods used for its calculation, providing a foundational accounting context.

May/June 2021

2. Which of the following topics is NOT included in the structural outline of the chapter on 'Depreciation and its Accounting'?
   (A) Revaluation of Fixed Assets
   (B) Sum of the Years' Digits Method
   (C) Amortisation of intangible assets
   (D) Replacement of a Fixed Asset and Creation of Sinking Fund

   Ans :

   (A) Revaluation of Fixed Assets
   A review of the chapter's structure, as provided on the first page, indicates a comprehensive discussion on various depreciation methods, amortisation, and asset replacement. However, the specific topic of 'Revaluation of Fixed Assets' is not listed as a distinct section, making it the correct answer as it falls outside the chapter's stated scope.

Oct/Nov 2005

3. What is one of the primary learning objectives of this unit on depreciation?
   (A) To understand asset valuation specifically for obtaining insurance coverage
   (B) To analyze the impact of depreciation exclusively on cash flow from operating activities
   (C) To learn how to prepare a depreciation account and understand the related accounting entries
   (D) To master the complex legal requirements for asset disposal across various regulated industries

   Ans :

   (C) To learn how to prepare a depreciation account and understand the related accounting entries
   The 'Objectives' section clearly states that a goal of the unit is to understand how to prepare a depreciation account and the accounting entries passed for recording depreciation. This highlights the practical accounting skills the chapter aims to impart, focusing on the procedural aspects of recording the reduction in an asset's value over time.

May/June 2010

4. How does the Institute of Chartered Accountants of England and Wales define the provision against the loss of capital due to depreciation?
   (A) A discretionary charge against profits, adjusted based on business profitability
   (B) A specific reserve created to fund future business expansion or new asset acquisitions
   (C) A non-operating expense that is only recorded upon the final sale or disposal of the asset
   (D) An integral cost of conducting the business, not dependent on profit earned

   Ans :

   (D) An integral cost of conducting the business, not dependent on profit earned
   The definition provided explicitly states that the provision against the loss of capital from depreciation is an "integral cost of conducting the business... and is not dependent upon the

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available to purchase a new asset when the old one is retired.

Oct/Nov 2006

15. For the purpose of calculating depreciation, which of the following is NOT considered one of the three basic factors?
(A) The market value of the asset during its life
(B) The cost of the asset
(C) The estimated residual or scrap value
(D) The estimated number of years of its useful life

Ans :

(A) The market value of the asset during its life
The chapter explicitly lists three basic factors for calculating depreciation: the cost of the asset, its estimated residual or scrap value, and its estimated useful life. The fluctuating market value of the asset during its operational life is not used in the standard calculation of depreciation, which is a systematic allocation of cost, not a valuation exercise.

May/June 2021

16. When determining the 'estimated useful life' of an asset for depreciation purposes, what is the crucial consideration for a firm?
(A) The total number of years the asset can physically run
(B) The number of years the asset is likely to be used by the firm
(C) The warranty period provided by the manufacturer
(D) The average lifespan of similar assets in the industry

Ans :

(B) The number of years the asset is likely to be used by the firm
The text clarifies that one should not consider the asset's maximum physical lifespan. Instead, the focus should be on the period it is likely to be used by the firm, which can be shorter due to factors like obsolescence from new inventions. The example of a machine with a 10-year physical life but an 8-year expected use illustrates this point.

Oct/Nov 2010

17. What is the standard accounting entry to record depreciation when the asset's value is directly reduced in the books?
(A) Debit Asset Account, Credit Depreciation Account
(B) Debit Depreciation Account, Credit Asset Account
(C) Debit Profit & Loss Account, Credit Asset Account
(D) Debit Asset Account, Credit Provision for Depreciation Account

Ans :

(B) Debit Depreciation Account, Credit Asset Account
The first method shown for recording depreciation involves directly crediting the asset account to reduce its book value. The corresponding debit is to the Depreciation Account, which is an expense. This entry, Depreciation Account Dr. To Asset Account`, reflects the consumption of the asset's value and is the standard entry for this direct reduction method.

May/June 2005

18. What is the alternative accounting entry for providing depreciation, which keeps the asset at its original cost in the ledger?
(A) Debit Depreciation Account, Credit Provision for Depreciation Account
(B) Debit Depreciation Account, Credit Asset Account
(C) Debit Profit & Loss Account, Credit Depreciation Account
(D) Debit Provision for Depreciation Account, Credit Asset Account

Ans :

(A) Debit Depreciation Account, Credit Provision for Depreciation Account
The chapter presents an alternative entry: `Depreciation Account Dr. To Provision for Depreciation Account`. This method does not reduce the asset account directly. Instead, it accumulates the depreciation in a separate liability/contra-asset account called 'Provision for Depreciation', allowing the asset account to reflect its original cost throughout its life on the ledger.

Oct/Nov 2022

19. If a company maintains a 'Provision for Depreciation Account', how is the asset's value presented in the Balance Sheet?
(A) At its original historical cost, without any deduction for depreciation
(B) At its current net realizable value, based on

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asset outdated or non-functional for its intended purpose. This type of value loss is not due to physical deterioration but rather to technological advancements or changes in consumer preferences, making the asset economically unviable.

May/June 2007

10. Which of the following is NOT listed as a primary cause of depreciation?
(A) Planned maintenance and servicing
(B) Accidents
(C) Fall in market price
(D) Obsolescence

Ans :

(A) Planned maintenance and servicing
The chapter lists five main causes of depreciation: wear and tear, efflux of time, obsolescence, accidents, and a fall in market price. Planned maintenance and servicing are activities intended to preserve an asset's value and functionality, not a cause of its depreciation, making this the correct exception from the provided list.

Oct/Nov 2025

11. While most assets typically diminish in value, which of the following asset types are mentioned in the chapter as having the potential to appreciate?
(A) Machinery and vehicles
(B) Computers and office equipment
(C) Buildings and furniture
(D) Land and old paintings

Ans :

(D) Land and old paintings
The chapter makes a specific exception to the general rule of depreciation by stating that "Only in a few cases, assets do appreciate." It then provides 'Land and old paintings' as explicit examples of assets that may go up in value over time, contrasting them with the usual continuous diminishment in the value of other assets.

May/June 2012

12. What is the primary reason for providing depreciation to ascertain the correct profit or loss?
(A) To create a fund for asset replacement
(B) Because the loss in asset value contributes to earning income
(C) To comply with tax regulations only
(D) To show a higher value of assets on the balance sheet

Ans :

(B) Because the loss in asset value contributes to earning income
The text states that the ascertainment of correct profit or loss is not possible without providing for depreciation. This is because the loss in the value of assets, which are used to generate revenue, is an expense that "goes towards earning of the income." Therefore, it must be matched against the revenues of the period.

Oct/Nov 2019

13. To present a 'true and fair' financial position, at what value should fixed assets be shown on the balance sheet for a going concern?
(A) Original cost
(B) Market value
(C) Cost less depreciation on account of use
(D) Replacement cost

Ans :

(C) Cost less depreciation on account of use
The chapter explains that for a balance sheet to show a true and fair view, fixed assets must be presented at their proper value. This proper value is defined as the original cost less the amount lost through wear and tear, which is the depreciation charged for the use of the asset during the period.

May/June 2019

14. Which of the following is a primary objective achieved by providing for depreciation?
(A) To increase the reported net profit for the period
(B) To avoid the need for any repairs on the asset
(C) To maintain the asset's market value equal to its book value
(D) To make provision for the future replacement of the asset

Ans :

(D) To make provision for the future replacement of the asset
One of the three key needs for depreciation mentioned is 'To make provision for replacement of asset'. The gradual decline in an asset's value necessitates its eventual replacement. By charging depreciation, a portion of the profits is retained in the business, implicitly making funds

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(C) ₹3,200.00

According to the table, the year-end value after Year 1 is ₹16,000. For Year 2, depreciation is calculated on this declining balance. At a 20 % rate, the depreciation is 20% times ₹16,000.00 = ₹3,200.00 . The table confirms this amount, showing how the method applies the rate to the residual value.

Oct/Nov 2021

34. From the 'Declining Balance Illustration', what is the year-end value of the asset at the end of Year 3?

"Declining Balance Illustration" table showing depreciation of an asset with a ₹20,000 original cost and 20 % depreciation rate.

(A) ₹12,800.00
(B) ₹8,192.00
(C) ₹2,560.00
(D) ₹10,240.00

Ans :

(D) ₹10,240.00

The illustration table clearly lays out the values for each year. For Year 3, the depreciation amount is listed as ₹2,560.00, and the corresponding "Year-end Value" is explicitly stated as ₹10,240.00. This value is derived by subtracting the Year 3 depreciation from the Year 2 end value (₹12,800.00 - ₹2,560.00).

May/June 2024

35. In the 'Declining Balance Illustration', the calculation for Year 2 depreciation is shown as ` [₹ 16,000.00/5] = ₹ 3,200.00`. What does the division by 5 represent in this context?

(A) A method to calculate a 20 % depreciation rate
(B) The useful life of the asset in years
(C) A typographical error in the formula
(D) The number of assets being depreciated

Ans :

(A) A method to calculate a 20 % depreciation rate

The problem states a depreciation rate of 20 %. The fraction $\frac{1}{5}$ is mathematically equivalent to 20% (or 0.20). The calculation `₹16,000.00 / 5` is an alternative way of writing `$16,000.00 \times \frac{1}{5}$` or `₹16,000.00 × 20%`. Therefore, the division by 5 is simply the application of the specified 20% annual depreciation rate.

Oct/Nov 2008

36. In the 'Declining Balance Illustration', with an original cost of ₹20,000 and a 20 % depreciation rate, what is the book value of the asset at the beginning of Year 5?

(A) ₹10,240.00
(B) ₹8,192.00
(C) ₹6,553.60
(D) ₹12,800.00

Ans :

(B) ₹8,192.00

The book value at the beginning of any year is the same as the year-end value of the preceding year. According to the provided table, the 'Year-end Value' at the end of Year 4 is ₹8,192.00. Therefore, this becomes the opening balance or the book value at the beginning of Year 5.

May/June 2006

37. Compared to the Straight Line Method, how is the charge to the Profit & Loss account structured under the Written Down Value method over the life of an asset?

(A) It is constant in all years
(B) It is higher in the initial years and lower in the later years
(C) It is lower in the initial years and higher in the later years
(D) It is charged only in the final year of the asset's life

Ans :

(B) It is higher in the initial years and lower in the later years

The text explicitly states that under the WDV method, "More depreciation tends to occur earlier in the asset's life." It further clarifies that "the charge to the Profit & Loss account is higher in initial years as compared to the later years of life of such asset," which is the defining financial impact of this method.

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Oct/Nov 2017

38. If Patel Transport used the Written Down Value (WDV) method at 10 % for its truck, what would be the depreciation for the year ending 31st March 2021? The book value on 1st April 2020 was ₹3,80,000.

(A) ₹38,000
(B) ₹40,000
(C) ₹20,000
(D) ₹34,200

estimated selling price
(C) At its original cost, with the provision for depreciation deducted to show the net value
(D) Omitted entirely from the balance sheet until the point of its final disposal

Ans :

(C) At its original cost, with the provision for depreciation deducted to show the net value
When a Provision for Depreciation Account is used, the asset continues to be shown at its original cost in the balance sheet. The accumulated depreciation in the provision account is then shown as a deduction from this cost. This presentation clearly displays the original investment, the total depreciation to date, and the resulting net book value.

May/June 2018

20. Which of the following is identified as the 'fixed instalment or straight line method'?
(A) Fixed percentage on diminishing balance
(B) Units of production method
(C) Sum of the years' digits method
(D) Fixed percentage on original cost

Ans :

(D) Fixed percentage on original cost
The chapter introduces the methods of depreciation and explicitly names the first one as 'Fixed percentage on original cost or fixed instalment or straight line method'. This name reflects the core mechanism of the method, where a constant amount or percentage of the initial cost is charged as depreciation each year.

Oct/Nov 2016

21. What is the fundamental assumption underlying the Straight Line Method (SLM) of depreciation?
(A) The asset depreciates more in its early years.
(B) The asset's depreciation is directly proportional to its usage.
(C) The asset will lose an equal amount of value each year.
(D) The asset's value will never reduce to its scrap value.

Ans :

(C) The asset will lose an equal amount of value each year.
The text clearly states that the Straight Line Method "assumes that the asset will lose an equal amount of value each year." This results in a constant depreciation expense being charged to the Profit & Loss account annually over the asset's useful life. This even distribution is the defining characteristic of the SLM.

May/June 2014

22. What is the correct formula for calculating annual depreciation under the Straight Line Method?
(A) $\frac{\text{Cost price of asset}}{\text{Estimated life of the asset}}$
(B) $\frac{\text{Cost price of asset} - \text{Scrap value}}{\text{Estimated life of the asset}}$
(C) $(\text{Cost price of asset} - \text{Scrap value}) \times \text{Depreciation Rate}$
(D) $\frac{\text{Scrap value}}{\text{Estimated life of the asset}}$

Ans :

(B) $\frac{\text{Cost price of asset} - \text{Scrap value}}{\text{Estimated life of the asset}}$
The chapter provides the precise formula for the Straight Line Method. It states that annual depreciation is calculated by subtracting the salvage (scrap) value from the purchase price (cost) and then dividing this depreciable amount by the estimated useful life of the asset in years. This ensures the cost is spread evenly.

Oct/Nov 2007

23. The Straight Line Method is considered particularly relevant for assets like Plant and Machinery under what condition?
(A) When they are projected to incur increasingly high repair costs in later years
(B) When they are susceptible to rapid technological obsolescence
(C) When their market resale value is known to fluctuate significantly
(D) When they are expected to give constant or consistent performance over their useful life

Ans :

(D) When they are expected to give constant or consistent performance over their useful life
The text suggests that SLM is more relevant for assets such as Plant and Machinery that are "expected to give constant/consistent performance over an extended period of time over the useful life." The logic is that if the asset contributes evenly to revenue generation each year, the cost should also be allocated evenly.

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amount of profit earned." This emphasizes that depreciation is a fundamental operating expense that must be accounted for regardless of the firm's profitability during the period.

Oct/Nov 2022

5. Which of the following is a key fact about depreciation highlighted by its formal definition?
(A) It is an appreciation in the value of an asset
(B) The decrease in value is sudden and unpredictable
(C) It represents a gradual and continuous reduction in asset value
(D) It is considered a part of the financing cost

Ans :

(C) It represents a gradual and continuous reduction in asset value
The chapter outlines four key facts derived from the definition of depreciation. One of these is that the decrease in the value of an asset is gradual and continuous. This characteristic distinguishes depreciation from other sudden losses in value, such as those caused by accidents, and underlines its nature as a systematic allocation of cost over time.

May/June 2016

6. **Assertion (A) :** Depreciation is considered a part of the operating cost of a business.
Reason (R) : The decrease in the value of an asset is due to its use, wear and tear, or other reasons related to business operations.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A)
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A)
(C) (A) is true but (R) is false
(D) (A) is false but (R) is true

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A)
Depreciation is an operating cost because it represents the consumption of an asset's economic value in the process of generating revenue. The reason (R) correctly identifies that this value decrease stems from operational factors like usage and wear and tear. Therefore, the reason directly explains why depreciation is classified as an operating cost for the business.

NODIA

Oct/Nov 2009

7. What is the primary cause of depreciation that results directly from the physical usage of an asset?
(A) Obsolescence
(B) Efflux of time
(C) Fall in market price
(D) Wear and tear

Ans :

(D) Wear and tear
The chapter explicitly lists 'Wear and tear due to actual use' as the first and one of the main causes of depreciation. This refers to the physical deterioration of an asset that occurs as a direct consequence of its operation in the business, such as a machine's parts wearing out from running to produce goods.

May/June 2023

8. The reduction in an asset's value simply due to the passage of time, irrespective of its usage, is referred to as:
(A) Efflux of time
(B) Obsolescence
(C) Accidental damage
(D) Market fluctuation

Ans :

(A) Efflux of time
The chapter identifies 'Efflux of time' as a distinct cause of depreciation. It explains that the mere passage of time can cause a fall in an asset's value, even if it is not used. The example of a car bought in 1972 having negligible value in 2022, regardless of use, illustrates this specific concept perfectly.

Oct/Nov 2018

9. What is the term for the cause of depreciation that occurs when a new invention or a permanent change in demand makes an existing asset useless?
(A) Wear and tear
(B) Efflux of time
(C) Obsolescence
(D) Accidents

Ans :

(C) Obsolescence
The text defines 'Obsolescence' as a cause of depreciation where a new invention or a permanent shift in market demand renders an

May/June 2017

29. As shown in the Depreciation Account for Patel Transport, the balance of the depreciation charged each year is transferred to which account?
(A) Balance Sheet
(B) Truck Account
(C) Profit and Loss Account
(D) Bank Account

Ans :

(C) Profit and Loss Account
The Depreciation Account is a nominal account representing an expense. The ledger provided shows that at the end of each financial year (31-3-20, 31-3-21, 31-3-22), the amount debited to the Depreciation Account is transferred to the credit side as 'By Profit and Loss a/c'. This closes the depreciation account and charges the expense against revenues.

Oct/Nov 2005

30. What is the defining characteristic of the Diminishing Balance or Written Down Value (WDV) method?
(A) Charging a fixed and constant amount of depreciation every year
(B) Applying a fixed depreciation rate to the asset's original historical cost
(C) Ensuring the asset is fully written down to zero value before its life ends
(D) The depreciation rate is applied to the residual or opening balance of the asset

Ans :

(D) The depreciation rate is applied to the residual or opening balance of the asset
The WDV method is defined as a method where the percentage rate is applied to the residual balance (written down value) of the asset from the previous year, rather than to the original cost. This results in a depreciation amount that is highest in the first year and diminishes in subsequent years.

May/June 2020

31. How is the annual depreciation calculated under the Written Down Value (WDV) method, as per the equation provided?
(A) Previous year's value × Percentage rate
(B) Original cost × Percentage rate
(C) (Original cost - Scrap value) × Percentage rate
(D) (Previous year's value - Scrap value) × Percentage rate

Ans :

(A) Previous year's value × Percentage rate
The chapter provides a clear equation for this method:

$$\text{Annual Depreciation} = \text{Previous year's value} \times \text{Percentage rate}$$

This formula is the core of the WDV method, ensuring that the depreciation charge is based on the book value of the asset at the beginning of the accounting period, leading to a declining expense over time.

Oct/Nov 2015

32. The Written Down Value (WDV) method is considered more relevant for assets which are expected to:
(A) Provide a stable and consistent level of performance throughout their life
(B) Give better performance in the initial periods of use
(C) Incur minimal repair and maintenance costs during their later years
(D) Tend to appreciate, rather than depreciate, in market value over time

Ans :

(B) Give better performance in the initial periods of use
The text explicitly states that the WDV method is more relevant for assets like Vehicles, Computers, and Office Equipment that are "expected to give better performance in the initial periods of use as compared to the later." This aligns with charging higher depreciation in the early, more productive years of the asset's life.

May/June 2013

33. Based on the 'Declining Balance Illustration' provided, what is the calculated depreciation amount for Year 2?
"Example; If the original cost of an asset is ₹20,000 and the rate of depreciation is 20 %, the following table describes how the declining balance would depreciate the asset."
(A) ₹4,000.00
(B) ₹2,560.00
(C) ₹3,200.00
(D) ₹16,000.00

Ans :

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May/June 2025

24. Patel Transport acquired a truck for ₹4,00,000 on 1st October 2019. The firm uses the Straight Line Method at 10 % on original cost and closes its books on 31st March. What is the depreciation amount for the year ending 31st March 2020?
(A) ₹20,000
(B) ₹40,000
(C) ₹10,000
(D) ₹30,000

Ans :

(A) ₹20,000
The annual depreciation is 10 % of ₹4,00,000, which equals ₹40,000. However, the asset was acquired on 1st October 2019 and used for only 6 months in the financial year ending 31st March 2020 (October to March).
Therefore, the depreciation for this period is for 6 months:

$$40,000 \times \frac{6}{12} = 20,000.$$

May/June 2009

25. In the Patel Transport illustration using the Straight Line Method, what is the depreciation charge for the full financial year ending 31st March 2021?
(A) ₹20,000
(B) ₹38,000
(C) ₹40,000
(D) ₹36,000

Ans :

(C) ₹40,000
Under the Straight Line Method, depreciation is calculated on the original cost. The annual depreciation is 10 % of the original cost of ₹4,00,000, which is ₹40,000. For the full financial year from 1st April 2020 to 31st March 2021, the entire annual depreciation amount is charged, as the asset was used for the whole year.

Oct/Nov 2011

26. Following the Patel Transport illustration (SLM), what is the closing balance (Balance c/d) of the Truck Account as on 31st March 2022?
(A) ₹3,40,000
(B) ₹3,20,000
(C) ₹2,80,000
(D) ₹3,00,000

Ans :

(D) ₹3,00,000
The opening balance on 1-4-2021 is ₹3,40,000. The depreciation for the year ending 31-3-2022 is ₹40,000 (10 % of original cost ₹4,00,000). The closing balance is the opening balance minus the current year's depreciation: ₹3,40,000 - ₹40,000 = ₹3,00,000 . This is clearly shown in the Truck Account ledger in the illustration.

May/June 2010

27. In the Truck Account for Patel Transport shown in Illustration No. 1, what does the entry 'By Depreciation a/c' on the credit side signify?
(A) A reduction in the book value of the truck
(B) An increase in the truck's value
(C) The sale of the truck
(D) The purchase of a new truck

Ans :

(A) A reduction in the book value of the truck
In an asset account like the Truck Account, debits represent increases (purchase) and credits represent decreases. The credit entry 'By Depreciation a/c' signifies the allocation of a portion of the asset's cost as an expense for the period, thereby reducing its carrying or book value in the company's financial records as shown on the balance sheet.

Oct/Nov 2024

28. An asset is purchased on 1st January, and the company's financial year ends on 31st March. For how many months should depreciation be provided in the last year of the asset's estimated life span?
(A) Three months
(B) Nine months
(C) Six months
(D) Twelve months

Ans :

(B) Nine months
The chapter provides an example stating that if an asset is bought on 1st January and books close on 31st March, three months' depreciation is charged in the first year. Consequently, to complete the full useful life, the final depreciation charge in the last year of its life span will be for the remaining nine months.

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Ans :

(A) ₹38,000

Under the WDV method, the 10 % rate is applied to the opening balance of the asset for the year. The opening balance on 1st April 2020 (carried forward from 31st March 2020) is ₹3,80,000. Therefore, the depreciation for the full year 2020-21 is

$$10\% \times 3,80,000$$

$$= 38,000$$

As shown in the WDV illustration.

May/June 2008

39. As per the WDV method calculation for Patel Transport's truck, what is the closing balance (Balance c/d) of the truck account on 31st March 2022?

(A) ₹3,00,000
(B) ₹3,42,000
(C) ₹3,07,800
(D) ₹3,09,600

Ans :

(C) ₹3,07,800

The opening balance on 1st April 2021 is ₹3,42,000. Depreciation for the year 2021-22 is 10 % of this value, which is ₹34,200. The closing balance is calculated as the opening balance minus the depreciation for the year: ₹3,42,000 - ₹34,200 = ₹3,07,800 . This figure is explicitly shown in the WDV truck account illustration.

Oct/Nov 2013

40. Which of the following is highlighted as a primary advantage of the Straight Line Method of depreciation?

(A) It accurately reflects the pattern of asset usage
(B) It results in a higher tax shield in the early years
(C) It accounts for increasing repair costs in later years
(D) It is the simplest method of calculating depreciation

Ans :

(D) It is the simplest method of calculating depreciation

The chapter lists two main advantages for the Straight Line Method. The first one mentioned is that "It is the simplest method of calculating depreciation." The second advantage is that it is easy to understand due to the lack of variation in the annual depreciation amount, reinforcing the overall theme of simplicity for this method.

May/June 2015

41. Which of the following statements correctly identifies a key disadvantage of the Straight Line Method?

(A) It presents significant difficulties in its calculation and application
(B) The asset's book value is never fully depreciated down to a zero balance
(C) The total charge for depreciation and repairs increases in later years
(D) It is generally not a recognized method for income tax calculation purposes

Ans :

(C) The total charge for depreciation and repairs increases in later years

The main disadvantage cited for SLM is that while depreciation remains constant, repair and renewal expenditures increase as the asset ages. This results in a "higher amount charged to profit and loss account on account of depreciation and repairs in the subsequent years," creating an uneven total charge over the asset's life.

Oct/Nov 2012

42. A major criticism of the Straight Line Method is that the combined annual charge to the P&L account for depreciation and repairs tends to:

(A) Remain constant over the asset's life
(B) Increase as the asset gets older
(C) Decrease as the asset gets older
(D) Be unpredictable and random

Ans :

(B) Increase as the asset gets older

The chapter points out that under SLM, the depreciation charge is constant. However, repair costs typically rise as an asset ages. Therefore, the sum of the constant depreciation and the increasing repair costs results in a total charge to the P&L account that grows larger in the later years of the asset's life.

May/June 2011

43. Match the item from the WDV Truck Account illustration (List-I) with its corresponding amount in ₹ (List-II).

List-I

P. Depreciation for year ending 31-3-21

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(D) SLM uses original cost while WDV uses the book value at the beginning of the year.
The fundamental distinction lies in the base for calculation. The Straight Line Method consistently applies the depreciation rate to the asset's original cost. In contrast, the Written Down Value method applies the rate to the asset's book value (or residual balance), which decreases each year, leading to a declining depreciation charge.

Oct/Nov 2013

82. Match the depreciation method in List-I with its primary characteristic in List-II.
List-I (Method)
P. Straight Line Method
Q. Written Down Value Method
R. Units of Production Method
List-II (Characteristic)
1. Depreciation charge decreases each year.
2. Depreciation charge is based on asset usage.
3. Depreciation charge is constant each year.
(A) P-3, Q-1, R-2
(B) P-1, Q-3, R-2
(C) P-2, Q-1, R-3
(D) P-3, Q-2, R-1

Ans :

(A) P-3, Q-1, R-2
The Straight Line Method (P) is defined by its constant annual charge (3). The Written Down Value Method (Q) results in a declining or diminishing charge each year (1). The Units of Production Method (R) links the depreciation expense directly to the asset's activity level or usage (2). This matching correctly aligns each method.

May/June 2015

83. What is the primary subject matter dealt with by Indian Accounting Standard (Ind AS) 16?
(A) Intangible Assets
(B) Financial Instruments
(C) Accounting treatment for property, plant and equipment
(D) Revenue Recognition

Ans :

(C) Accounting treatment for property, plant and equipment
The annexure begins by stating that Ind AS 16 "deals with accounting treatment for property, plant and equipment." It elaborates that the main issues covered are the recognition of these assets, the determination of their carrying amounts, and the depreciation charges to be recognised in relation to them, confirming its focus.

Oct/Nov 2012

84. According to the salient features of Ind AS 16, how is the 'depreciable amount' of an asset determined?
(A) It is the cost of the asset only.
(B) It is the residual value of the asset.
(C) The average market value of the asset over its life.
(D) It is its cost, or other amount substituted for cost, less its residual value.

Ans :

(D) It is its cost, or other amount substituted for cost, less its residual value.
The first salient feature of Ind AS 16 listed in the annexure provides a precise definition. It states that the "Depreciable amount of a depreciable asset is its cost, or other amount substituted for cost in, less its residual value." This is the total value that will be systematically allocated over the asset's useful life.

May/June 2011

85. Ind AS 16 provides two alternative definitions for 'useful life'. One is the period over which an asset is expected to be available for use. What is the other definition?
(A) The number of production or similar units expected to be obtained from the asset.
(B) The warranty period given by the manufacturer.
(C) The period until the asset's market value falls to zero.
(D) The minimum period mandated by tax authorities.

Ans :

(A) The number of production or similar units expected to be obtained from the asset.
The annexure lists two ways to define useful life under Ind AS 16. The first is time-based (period of availability), and the second is usage-based: "The number of production or similar units expected to be obtained from the use of the asset by the entity." This aligns with the concept behind the Units of Production method.

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(B) Written Down Value Method
(C) Units of Production Method
(D) Sum of the Years' Digits Method

Ans :

(B) Written Down Value Method
The chapter explicitly lists "The assets are never fully depreciated" as the third disadvantage of the Written Down Value method. This is a direct consequence of its calculation, where each year's depreciation is a fraction of the remaining balance, which mathematically approaches zero but never reaches it, leaving a small book value.

Oct/Nov 2009

48. According to the text, which three methods of calculating depreciation are recognized by Accounting Standards in India (AS-10 and Ind AS-16)?
(A) Straight Line, Diminishing Balance, and Units of Production
(B) Straight Line, Annuity, and Sinking Fund
(C) Straight Line, Diminishing Balance, and Sum of the Years' Digits
(D) Diminishing Balance, Units of Production, and Annuity

Ans :

(A) Straight Line, Diminishing Balance, and Units of Production
In the section discussing the Units of Production method, the text explicitly states, "Accounting Standards in India (AS-10 and Ind AS-16) recognise 3 methods of calculating depreciation. These are Straight line method, Diminishing Balance method and the Units of Production method." This directly answers the question based on the provided content.

May/June 2023

49. The Units of Production method of depreciation is best described as a:
(A) Time-based method
(B) Value-based method
(C) Usage-based method
(D) Market-based method

Ans :

(C) Usage-based method
The chapter clearly defines this method as "a usage based method." It further elaborates that the depreciation amount is not based on the passage of time but on the actual use of the asset. This makes it fundamentally different from time-based methods like SLM and WDV, linking the expense directly to the asset's output or activity.

Oct/Nov 2018

50. For which type of assets is the Units of Production method most appropriate and suitable?
(A) Assets whose value declines mainly due to the passage of time, like buildings.
(B) Intangible assets like patents and copyrights.
(C) Assets that have high maintenance costs in their later years, like vehicles.
(D) Assets which depreciate in proportion to their use, like a production machine.

Ans :

(D) Assets which depreciate in proportion to their use, like a production machine.
The text states that this method is "suited to those assets which depreciate in proportion to their use rather than having a useful life measured in number of years." The useful life is measured in terms of production output, making it ideal for machinery or equipment whose wear and tear is directly related to its operational activity.

May/June 2007

51. Question 51. In this formula, what does the 'Total depreciable amount of the asset' represent?
"Depreciation amount during a period = $\frac{\text{Actual production}}{\text{Total Expected Production}} \times \text{Total depreciable amount of the asset}$"
(A) The asset's original, unadjusted purchase price from the vendor
(B) The asset's final estimated scrap or residual value at disposal
(C) The original cost minus the estimated scrap value
(D) The prevailing market value of the asset at the end of the financial year

Ans :

(C) The original cost minus the estimated scrap value
The total depreciable amount of any asset is the portion of its cost that will be allocated as an expense over its useful life. This is universally calculated as the asset's original cost minus its estimated residual or scrap value. The formula then allocates a fraction of this total depreciable amount based on the period's production.

NODIA

nature of the SYD method, which allocates a larger portion of the asset's cost as an expense in the initial years of its life.

Oct/Nov 2016

62. What is the primary purpose of creating a 'Depreciation Fund' or 'Sinking Fund' as described in the chapter?
(A) To pay for annual repairs and maintenance of the asset
(B) To have money available for the purchase of a new asset upon replacement
(C) To speculate in the securities market for additional profit
(D) To pay dividends to shareholders

Ans :

(B) To have money available for the purchase of a new asset upon replacement
The text explains that the Sinking Fund method is used to plan for the replacement of fixed assets. It involves setting aside cash equal to the yearly depreciation expense so that "money will be available to purchase a new asset once the current one is fully depreciated." This directly addresses the cash flow needs for asset replacement.

May/June 2014

63. Under the Sinking Fund method, what is done with the annual amount set aside for depreciation?
(A) It is kept as idle cash in a bank account.
(B) It is used to pay off existing company loans.
(C) It is invested in readily saleable securities.
(D) It is immediately used to buy parts for the existing asset.

Ans :

(C) It is invested in readily saleable securities.
The chapter specifies that under this method, a 'Depreciation Fund' or 'Sinking Fund' is created, and "the amount is invested in readily saleable securities." This investment strategy aims to earn a return on the funds set aside, with the securities being sold at the end of the asset's life to finance its replacement.

Oct/Nov 2007

64. What is the term for the systematic allocation of the depreciable amount of an intangible asset over its useful life?
(A) Depreciation
(B) Depletion
(C) Impairment
(D) Amortisation

Ans :

(D) Amortisation
The chapter explicitly states that reducing the value of intangible assets over their useful life is called "amortisation." It further clarifies that this process is similar to depreciation but is the specific term used for assets lacking physical substance. The definition from Ind AS 38 reinforces this, defining amortisation as the systematic allocation for intangible assets.

May/June 2025

65. This definition positions amortisation as a process that is conceptually analogous to which other accounting process?
"Indian Accounting Standard (Ind AS) 38, which deals with intangible assets, describes amortisation as under; 'Amortisation is the systematic allocation of the depreciable amount of an intangible asset over its useful life.'"
(A) Depreciation
(B) Valuation
(C) Capitalisation
(D) Liquidation

Ans :

(A) Depreciation
The definition of amortisation provided by Ind AS 38 mirrors the definition of depreciation almost exactly, with the key difference being the type of asset it applies to (intangible vs. tangible). The chapter itself states that amortisation "is similar to depreciation" and the discussion on depreciation is "equally applicable to amortization."

Oct/Nov 2019

66. Based on this definition from Ind AS 38, which item would NOT qualify as PPE?
"This Standard [Ind AS 38] defines an intangible asset as, 'an identifiable non-monetary asset without physical substance'."
(A) It must have physical substance.
(B) It must lack physical substance.
(C) It must be a monetary asset.
(D) It cannot be identifiable.

Ans :

(B) It must lack physical substance.
The definition provided directly from Ind AS 38 is very clear. A defining and mandatory

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asset's life." This classifies it as an accelerated depreciation method, where the expense recognized is front-loaded, contrasting with the even allocation of the straight-line method.

May/June 2021

57. For an asset with an estimated useful life of 10 years, what is the 'Sum of the years' digits' used for calculation in the SYD method?
(A) 10
(B) 55
(C) 100
(D) 45

Ans :

(B) 55
The method requires adding the digits representing the years of useful life. For a 10-year life, this is calculated as $10 + 9 + 8 + 7 + 6 + 5 + 4 + 3 + 2 + 1$. The sum of these numbers is 55, which is explicitly stated in the illustration provided in the chapter.

Oct/Nov 2010

58. For an asset with a 10-year useful life being depreciated using the SYD method, what fraction is applied to the depreciable base to calculate depreciation in the first year?
(A) $\frac{10}{55}$
(B) $\frac{1}{55}$
(C) $\frac{1}{10}$
(D) $\frac{9}{55}$

Ans :

(A) $\frac{10}{55}$

In the SYD method, the depreciation fraction for a given year uses the number of remaining years of life as the numerator and the sum of the years' digits as the denominator. For the first year of a 10-year asset, the remaining life is 10 years, and the sum of digits is 55. Thus, the fraction is $\frac{10}{55}$.

May/June 2005

59. A computer is acquired for ₹5,000 with a salvage value of ₹200 and a 3-year useful life. For calculating depreciation using the Sum of the Years' Digits method, what is the depreciable base of the computer?
(A) ₹5,000
(B) ₹5,200
(C) ₹4,800
(D) ₹200

Ans :

(C) ₹4,800
The depreciable base is the amount of the asset's cost that will be allocated over its life. It is calculated as the original cost minus the salvage value. In this case, it is ₹5,000 - ₹200 = ₹4,800 . This is the base amount to which the SYD fractions will be applied.

Oct/Nov 2022

60. For the computer in the illustration (depreciable base ₹4,800, life 3 years), what is the depreciation charge for the second year using the SYD method? The sum of years' digits is 6 (3+2+1).
(A) ₹2,400.00
(B) ₹1,599.84
(C) ₹800.16
(D) ₹1,600.00

Ans :

(B) ₹1,599.84
For a 3-year life, the sum of digits is 3+2+1=6. The fraction for the second year is $\frac{2}{6}$.
The depreciation charge is

$$\frac{2}{6} \times 4{,}800 = 1{,}600$$

The text states ₹1,599.84, likely due to a rounding difference in the percentage (33.33 %). Based on the text's value, ₹1,599.84 is the correct answer.

May/June 2018

61. For the computer illustration, how does the depreciation charge in the first year under the SYD method (₹2,400) compare to the charge under the SLM (₹1,600)?
(A) The SYD charge is lower than the SLM charge.
(B) The comparison cannot be made from the given data.
(C) The SYD charge is significantly higher than the SLM charge.
(D) The SYD charge is equal to the SLM charge.

Ans :

(C) The SYD charge is significantly higher than the SLM charge.
The illustration explicitly calculates the first-year SYD depreciation as ₹2,400 and notes that the SLM charge would have been ₹1,600 per year. This comparison highlights the accelerated

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Q. Balance c/d on 31-3-21
R. Depreciation for year ending 31-3-22
S. Balance c/d on 31-3-22

List-II
1. 34,200
2. 3,07,800
3. 38,000
4. 3,42,000

(A) P-3, Q-4, R-1, S-2
(B) P-4, Q-3, R-2, S-1
(C) P-3, Q-1, R-4, S-2
(D) P-1, Q-2, R-3, S-4

Ans :

(A) P-3, Q-4, R-1, S-2
From the WDV Truck Account illustration:
P. Depreciation for 31-3-21 is ₹38,000.
Q. The closing balance on 31-3-21 is ₹3,42,000.
R. Depreciation for 31-3-22 is ₹34,200.
S. The final closing balance on 31-3-22 is ₹3,07,800.
This correctly matches the pairs as P-3, Q-4, R-1, and S-2.

Oct/Nov 2020

44. What is a key advantage of the Written Down Value method mentioned in the text?
(A) It is considered the simplest method to calculate and for stakeholders to understand
(B) It guarantees the asset's book value is fully depreciated to zero at life's end
(C) The amount of depreciation charged to the profit and loss account is constant annually
(D) It is a recognized method under the Ind AS-16, Income-Tax Act, and Companies Act

Ans :

(D) It is a recognized method under the Ind AS-16, Income-Tax Act, and Companies Act
The first advantage listed for the WDV method is its official recognition. The text explicitly states, "This method is one of the recognised methods under the Ind AS-16, Income-Tax Act and the Companies Act." This regulatory and standard-setting approval gives it significant weight and makes it a widely accepted practice in accounting.

May/June 2022

45. Under the Written Down Value method, why does the total annual expenditure on repairs and depreciation tend to be relatively stable over the years?
(A) In initial years, high depreciation is offset by low repairs, and in later years, low depreciation is offset by high repairs
(B) Both the annual depreciation charge and the expected repair costs remain constant over time
(C) The projected cost of future repairs is directly included in the annual depreciation calculation
(D) This depreciation method is exclusively applied to assets that require no repairs or maintenance

Ans :

(A) In initial years, high depreciation is offset by low repairs, and in later years, low depreciation is offset by high repairs
The chapter explains that under WDV, depreciation is higher in the initial years when repairs are less, and depreciation is lower in the later years when repairs are higher. This creates a balancing effect, leading to the total expenditure on both items tending to be relatively equal across all years of the asset's life.

Oct/Nov 2023

46. Which of the following is identified as a significant disadvantage of the Written Down Value (WDV) method?
(A) It is too simple and does not reflect the true consumption of the asset.
(B) The asset can never be reduced to zero value in the books.
(C) It results in a lower total depreciation charge over the asset's life compared to SLM.
(D) It is not recognized by major accounting standards.

Ans :

(B) The asset can never be reduced to zero value in the books.
The text lists three disadvantages of the WDV method. The first one mentioned is that "The asset can never be reduced to zero value in the books." Because the depreciation is a percentage of the remaining balance, there will always be a small residual value left, and the asset is never fully written off.

May/June 2016

47. The characteristic that an asset is "never fully depreciated" is a stated drawback of which depreciation method?
(A) Straight Line Method

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characteristic of an asset to be classified as intangible is that it must be "without physical substance." This is what distinguishes intangible assets like copyrights and patents from tangible assets like machinery and buildings.

May/June 2009

67. Which of the following is NOT provided as an example of an intangible asset in the chapter?
(A) Copyrights
(B) Accounts receivable
(C) Marketing rights
(D) Motion picture films

Ans :

(B) Accounts receivable
The chapter provides a list of examples of intangible assets, including scientific knowledge, copyrights, computer software, motion picture films, and marketing rights. Accounts receivable, however, is a monetary asset representing a claim to cash. It is not an intangible asset as defined by Ind AS 38, which specifies "non-monetary asset without physical substance."

Oct/Nov 2011

68. This description emphasizes that depreciation is primarily a process of:
"Depreciation accounting is described by AICPA as a system of accounting which aims to distribute the cost or other basic value of tangible capital asset less salvage value... in a systematic and rational manner. It is the process of allocation and not of valuation."
(A) Cost allocation
(B) Determining an asset's market worth
(C) Physical deterioration measurement
(D) Funding asset replacement

Ans :

(A) Cost allocation
The AICPA definition explicitly states that depreciation accounting is a process to "distribute the cost" of an asset over its useful life. It concludes with the crucial clarification that "It is the process of allocation and not of valuation." This means the goal is to spread the initial cost, not to reflect the asset's current market price.

May/June 2010

69. According to the 'LET US SUM UP' section, which tangible asset is noted as an exception for having a limited useful life?
(A) Building
(B) Machinery
(C) Land
(D) Vehicle

Ans :

(C) Land
The first point in the summary section states, "All tangible assets, except land, have limited useful life." This is a fundamental concept in accounting, as land is generally considered to have an indefinite life and is therefore not subject to depreciation, although it can be subject to impairment.

Oct/Nov 2024

70. The summary section lists four factors that affect the computation of depreciation. Which of the following is NOT one of those four factors?
(A) The prevailing interest rate
(B) Cost
(C) Residual value
(D) Estimated useful life

Ans :

(A) The prevailing interest rate
The 'LET US SUM UP' section clearly enumerates four factors: Cost, Residual value, Estimated useful life, and the Method of depreciation. The prevailing interest rate is not listed as a direct factor in the computation of depreciation itself, although it might be relevant in more complex valuation or investment decisions.

May/June 2017

71. In the summary of factors affecting depreciation, how is the 'Cost' of an asset defined?
(A) The net purchase price paid to the vendor, excluding any additional costs
(B) The manufacturer's suggested retail price (MSRP) before any discounts
(C) The trade-in value offered for an old asset being replaced by the new one
(D) Net purchase price plus all reasonable and necessary expenses to get the asset ready for use

Ans :

(D) Net purchase price plus all reasonable and necessary expenses to get the asset ready for use
The summary provides a detailed definition for 'Cost' as the "Net purchase price, including all reasonable and necessary expenses to get the asset

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Oct/Nov 2025

52. What is described as a significant drawback of the Units of Production method?
(A) It consistently provides an inaccurate measurement of an asset's depreciation
(B) The need to maintain elaborate records of production or usage
(C) It is a method that is not recognized by any major accounting standards
(D) Its application is restricted to assets with a useful life of less than five years

Ans :

(B) The need to maintain elaborate records of production or usage
The chapter mentions that while this method "gives very accurate measure of the depreciation," it "suffers from the drawback of the need to maintain elaborate records." This administrative burden of tracking the actual usage or production units for each asset is its main practical disadvantage compared to simpler time-based methods like SLM.

May/June 2012

53. Company ABC Ltd. purchases a pen production machine for ₹100,000. The scrap value is estimated at ₹10,000, and its total lifetime production capacity is 1,000,000 pens. What is the total depreciable amount of this machine?
(A) ₹100,000
(B) ₹10,000
(C) ₹90,000
(D) ₹110,000

Ans :

(C) ₹90,000
The total depreciable amount is the cost of the asset minus its estimated scrap value. In this case, it is the purchase price of ₹100,000 less the scrap value of ₹10,000. Therefore, the total amount that will be depreciated over the machine's life is ₹100,000 - ₹10,000 = ₹90,000 .

Oct/Nov 2014

54. In the ABC Ltd. example, the machine has a depreciable amount of ₹90,000 and a total capacity of 1,000,000 pens. If the machine produced 200,000 pens in the first year, what is the depreciation amount for that year?
(A) ₹10,000
(B) ₹20,000
(C) ₹90,000
(D) ₹18,000

Ans :

(D) ₹18,000
The depreciation is calculated based on the proportion of usage.
The fraction of capacity used is

$$\frac{200,000}{1,000,000}$$

Which is 0.2. The depreciation amount is this fraction multiplied by the total depreciable amount: $0.2 \times ₹90,000 = ₹18,000$. This calculation is shown explicitly in the example.

May/June 2019

55. Using the data for ABC Ltd.'s machine (depreciable amount ₹90,000, total capacity 1,000,000 pens), what would be the depreciation charge for the second year if the machine produced 150,000 pens?
(A) ₹13,500
(B) ₹18,000
(C) ₹15,000
(D) ₹9,000

Ans :

(A) ₹13,500
First, calculate the depreciation rate per unit:

$$\frac{90,000}{1,000,000 \text{ pens}} = 0.09 \text{ per pen.}$$

For the second year, the production is 150,000 pens. The depreciation charge is the production quantity multiplied by the rate per unit:
$150,000 \times ₹0.09 = ₹13,500$.

Oct/Nov 2006

56. What is the core assumption of the Sum of the Years' Digits (SYD) method of calculating depreciation?
(A) It assumes depreciation is constant each year.
(B) It assumes a higher depreciation charge and greater tax benefit in the early years.
(C) It assumes a lower depreciation charge in the early years.
(D) It assumes depreciation is linked to production volume.

Ans :

(B) It assumes a higher depreciation charge and greater tax benefit in the early years.
The chapter describes the SYD method as one that "assumes a higher depreciation charge and a greater tax benefit in the early years of an

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May/June 2024

77. The statement "Depreciation is like an insurance expense" is suggested to be untrue. What is a key difference between depreciation and an insurance expense?
(A) Insurance is a cash expense, while depreciation is a non-cash expense.
(B) Insurance protects against future loss, while depreciation accounts for past cost allocation.
(C) Insurance is an operating cost, while depreciation is not.
(D) Insurance is paid monthly, while depreciation is calculated annually.

Ans :

(B) Insurance protects against future loss, while depreciation accounts for past cost allocation.
While both can be operating expenses, their nature is different. Insurance is a payment made to a third party to protect against potential future risks and losses. Depreciation, however, is an internal accounting process of allocating the historical cost of an asset that has already been acquired. It is not a payment for future protection.

Oct/Nov 2008

78. The process of recording depreciation directly causes a reduction in which value of an asset?
(A) Book value
(B) Market value
(C) Scrap value
(D) Replacement value

Ans :

(A) Book value
Depreciation is an accounting entry that systematically reduces the carrying amount of a fixed asset in the company's books. This carrying amount is known as the book value (Cost - Accumulated Depreciation). While depreciation may be correlated with a fall in market value, its direct and intended effect is on the book value.

May/June 2006

79. As per the text, which combination of depreciation methods is explicitly recognized by Accounting Standards in India (AS-10 and Ind AS-16)?
(A) Straight line, Annuity, and Sinking Fund methods
(B) Diminishing Balance, Sum of the Years' Digits, and Annuity methods
(C) Straight line, Diminishing Balance, and Units of Production method
(D) Straight line, Diminishing Balance, and Sum of the Years' Digits method

Ans :

(C) Straight line, Diminishing Balance, and Units of Production method
The chapter, when introducing the Units of Production method, clearly states that "Accounting Standards in India (AS-10 and Ind AS-16) recognise 3 methods of calculating depreciation. These are Straight line method, Diminishing Balance method and the Units of Production method." This provides a definitive list based on the standards mentioned.

Oct/Nov 2017

80. Consider the following statements:
1. The Straight Line Method results in a constant annual depreciation charge.
2. The Written Down Value Method applies the depreciation rate to the original cost of the asset each year.

Which of the above statements is/are correct?
(A) Only 1
(B) Only 2
(C) Both 1 and 2
(D) Neither 1 nor 2

Ans :

(A) Only 1
Statement 1 is correct; the SLM is also known as the fixed instalment method because the depreciation expense is the same every year. Statement 2 is incorrect; the WDV method applies the depreciation rate to the written-down or residual balance of the asset, not the original cost. The original cost is used in the SLM.

May/June 2008

81. What is the primary difference in the calculation base used between the Straight Line Method (SLM) and the Written Down Value (WDV) method?
(A) SLM uses original cost while WDV uses market value.
(B) SLM uses scrap value while WDV uses original cost.
(C) There is no difference in the calculation base, only in the rate.
(D) SLM uses original cost while WDV uses the book value at the beginning of the year.

Ans :

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in place and ready for use." This comprehensive definition includes not just the price but also costs like freight, installation, and taxes that are essential to make the asset operational.

Oct/Nov 2005

72. The 'Estimated useful life' of a long-term asset, as a factor in depreciation, may be measured in which of the following units?
(A) Years only
(B) Years, units, miles, etc.
(C) Currency units only
(D) Percentage points only

Ans :

(B) Years, units, miles, etc.
The summary clarifies that the 'Estimated useful life' is the total number of service units expected from an asset. It explicitly states that this can be measured in various ways, including "in years, units, miles, etc." This allows for flexibility to match the measurement unit to the nature of the asset being depreciated.

May/June 2020

73. In which method of calculating depreciation is the amount of annual expense directly dependent on the volume of production or usage?
(A) Straight Line Method
(B) Written Down Value Method
(C) Units of Production Method
(D) Sum of the Years' Digits Method

Ans :

(C) Units of Production Method
The Units of Production method is unique because it is a usage-based method. The depreciation expense for a period is not determined by the passage of time but by the actual output or activity level of the asset, such as the number of units produced or miles driven, making it dependent on production volume.

Oct/Nov 2015

74. Which depreciation method involves charging a fixed percentage on the diminishing value of the asset each year?
(A) Straight Line Method
(B) Sinking Fund Method
(C) Units of Production Method
(D) Written Down Value Method

Ans :

(D) Written Down Value Method
The Written Down Value (WDV) or Diminishing Balance method is defined by its application of a fixed percentage rate to the book value (or written down value) of the asset at the beginning of each period. This results in a depreciation charge that decreases each year as the asset's book value diminishes.

May/June 2013

75. A 'Check Your Progress' question asks to identify a statement that is not true. One option is "Depreciation is not a part of the operating costs." Why is this statement factually incorrect?
(A) Because depreciation is an integral cost of conducting business to earn revenue
(B) Because depreciation is a financing cost
(C) Because depreciation is a non-cash expense and therefore not a cost
(D) Because depreciation is only recorded when an asset is sold

Ans :

(A) Because depreciation is an integral cost of conducting business to earn revenue
The definition from the Institute of Chartered Accountants of England and Wales, quoted in the chapter, explicitly calls the provision for depreciation "an integral cost of conducting the business." It represents the cost of using a fixed asset to generate revenue, and is therefore a fundamental part of a company's operating costs.

Oct/Nov 2021

76. Identify the incorrect statement regarding the nature of depreciation.
(A) Depreciation is an expense charged to the Profit & Loss account.
(B) All assets are depreciated at the same rate.
(C) Depreciation is a part of the operating costs.
(D) Depreciation is the process of cost allocation.

Ans :

(B) All assets are depreciated at the same rate.
The statement that all assets are depreciated at the same rate is incorrect. Different assets have different useful lives, scrap values, and patterns of economic benefit consumption. Consequently, firms use different rates and even different methods (SLM, WDV, etc.) for various classes of assets to accurately reflect their individual depreciation patterns.

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Oct/Nov 2020

86. Based on this definition from Ind AS 16, which item would NOT qualify as PPE?
"Property, plant and equipment are tangible items which; (i) are expected to be used during more than one accounting period; and (ii) are held by an enterprise for use in the production or supply of goods and services, for rental to others, or for administrative purposes and not for the purpose of sale in the ordinary course of business."
(A) A delivery van used for business operations over five years
(B) A plot of land held for resale by a real estate company
(C) An office building owned and used by the company for administration
(D) Manufacturing machinery used in production with a ten-year useful life

Ans :

(B) A plot of land held for resale by a real estate company
The definition explicitly states that PPE items are "not for the purpose of sale in the ordinary course of business." A plot of land held by a real estate company for resale is its inventory or stock-in-trade, not a fixed asset used in its operations. The other options fit the PPE definition.

May/June 2022

87. According to Ind AS 16, if a part of an item of property, plant, and equipment has a cost that is significant in relation to the total cost, what accounting treatment is required?
(A) It should be ignored for depreciation purposes.
(B) It shall be depreciated separately.
(C) It should be depreciated at the same rate as the main asset.
(D) It should be expensed immediately in the profit or loss account.

Ans :

(B) It shall be depreciated separately.
Point 5 of the salient features of Ind AS 16 states, "Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item, shall be depreciated separately." This component approach ensures a more accurate allocation of cost, especially for complex assets.

Oct/Nov 2023

88. Under the provisions of Ind AS 16, where should the depreciation charge for a period normally be recognized?
(A) In the profit or loss statement
(B) Directly in the balance sheet as a reduction of equity
(C) As an inflow in the cash flow statement
(D) In a separate reserve account not affecting profit

Ans :

(A) In the profit or loss statement
Point 6 under the features of Ind AS 16 specifies that "The depreciation charge for each period shall be recognised in profit or loss unless it is included in the carrying amount of another asset." This establishes depreciation as a standard expense to be matched against revenues for the period.

May/June 2016

89. Ind AS 16 mandates that the depreciation method selected by an entity should be applied consistently from period to period unless what occurs?
(A) There is a change in the company's management.
(B) The company reports a net loss for the year.
(C) There is a change in the expected pattern of consumption of future economic benefits.
(D) The tax laws for depreciation change.

Ans :

(C) There is a change in the expected pattern of consumption of future economic benefits.
Point 9 of the salient features of Ind AS 16 addresses consistency. It allows a change in method only if "there is a change in the expected pattern of consumption of future economic benefits." This means the accounting must follow the economic reality of how the asset's value is being used up.

Oct/Nov 2009

90. According to this disclosure requirement from Ind AS 16, what must a company report in its financial statements?
"The following information should be disclosed in the financial statements; (i) Depreciation methods used; and (ii) Depreciation rates or the useful lives of the assets."
(A) The specific depreciation methods and rates

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lack physical substance. Both are conceptually similar cost allocation processes.

May/June 2011

127. Identify the incorrect statement among the following regarding depreciation accounting principles.

(A) The cost of an asset includes all necessary expenses to make it ready for use.

(B) The Written Down Value method results in a constant annual depreciation charge.

(C) Depreciation is a process of cost allocation, not valuation.

(D) Land is generally not subject to depreciation.

Ans :

(B) The Written Down Value method results in a constant annual depreciation charge.

This statement is incorrect. The Written Down Value (WDV) method, by its very nature, results in a declining or diminishing annual depreciation charge. It is the Straight Line Method (SLM) that produces a constant annual depreciation charge. All other statements are correct principles discussed in the chapter.

Oct/Nov 2020

128. Consider the following depreciation methods:

1. Straight Line Method
2. Written Down Value Method
3. Sum of the Years' Digits Method
4. Units of Production Method

Which of these are generally considered accelerated depreciation methods?

(A) 2 and 3 (B) 1 and 4

(C) 1 and 2 (D) 3 and 4

Ans :

(A) 2 and 3

Accelerated depreciation methods charge more depreciation in the early years of an asset's life. The Written Down Value (WDV) method and the Sum of the Years' Digits (SYD) method both follow this pattern. The Straight Line Method provides a constant charge, and the Units of Production method's charge varies with usage, not time.

May/June 2022

129. Match the Accounting Standard (List-I) with its primary area of focus (List-II) as discussed in the chapter.

List-I (Standard)

P. Ind AS 16

Q. Ind AS 38

R. AS 10

List-II (Focus)

1. Intangible Assets
2. Property, Plant and Equipment

(A) P-2, Q-1, R-2

(B) P-1, Q-2, R-2

(C) P-2, Q-1, R-1

(D) P-1, Q-2, R-1

Ans :

(A) P-2, Q-1, R-2

As per the annexure, both Ind AS 16 (P) and AS 10 (R) prescribe the accounting treatment for Property, Plant and Equipment (2). Ind AS 38 (Q) specifically deals with the accounting treatment for Intangible Assets (1). Therefore, the correct matching is P-2, Q-1, and R-2.

Oct/Nov 2023

130. Which of the following is an incorrect statement concerning the provisions of AS-10 regarding Property, Plant and Equipment?

(A) The cost of PPE is recognized if future economic benefits are probable and cost is measurable.

(B) PPE acquired in exchange for a non-monetary asset should be valued at the book value of the asset given up.

(C) The residual value and useful life of an asset should be reviewed at each balance sheet date.

(D) Costs of day-to-day servicing are not capitalized as part of PPE.

Ans :

(B) PPE acquired in exchange for a non-monetary asset should be valued at the book value of the asset given up.

This statement is incorrect. AS-10 specifies that PPE acquired in such an exchange is generally to be valued at fair value, not the book value of the asset being exchanged. The other statements correctly reflect the provisions for recognition, review of estimates, and treatment of subsequent costs as outlined in the chapter's annexure on AS-10.

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guiding standard for tangible fixed assets under this framework.

May/June 2012

95. How does AS-10 define Property, Plant and Equipment (PPE) in terms of their expected period of use?
(A) They are expected to be used for exactly twelve months.
(B) They are expected to be used during more than a period of twelve months.
(C) They are expected to be used for less than a period of twelve months.
(D) The period of use is not a defining characteristic.

Ans :

(B) They are expected to be used during more than a period of twelve months.
The definition of PPE under AS-10 specifies that they are tangible items that, among other criteria, "are expected to be used during more than a period of twelve months." This long-term nature is what classifies them as non-current or fixed assets, distinguishing them from current assets like inventory.

Oct/Nov 2014

96. According to this recognition criteria from AS-10, what is the first condition for capitalizing a cost as PPE?
"The cost of an item of PPE should be recognised as an asset if, and only if: (a) it is probable that future economic benefits associated with the item will flow to the enterprise; and (b) the cost of the item can be measured reliably."
(A) The asset must be new.
(B) It must be probable that future economic benefits will flow to the enterprise.
(C) The cost must exceed a certain monetary threshold.
(D) The asset must have a physical form.

Ans :

(B) It must be probable that future economic benefits will flow to the enterprise.
The source text from AS-10 provides two mandatory conditions for recognition. The first condition, listed as (a), is the probability of future economic benefits flowing to the entity. This means the asset must be expected to contribute to future cash inflows or cost savings for the business to be placed on the balance sheet.

May/June 2019

97. As per AS-10, the cost of an item of PPE at recognition includes its purchase costs, directly attributable costs, and which other category of costs?
(A) Costs of day-to-day servicing
(B) Costs of dismantling and restoration
(C) General administrative overheads
(D) Costs of training staff to use the asset

Ans :

(B) Costs of dismantling and restoration
The section 'Measurement at recognition' under AS-10 breaks down the cost of PPE into three components: (a) purchase costs, (b) directly attributable and necessary costs, and (c) costs of dismantling and restoration. This third component refers to the estimated cost of removing the asset and restoring the site at the end of its life.

Oct/Nov 2006

98. According to the rules specified under AS-10, which type of subsequent costs are explicitly not recognised as part of PPE?
(A) Subsequent costs on day-to-day servicing
(B) Costs of site preparation
(C) Installation and assembly costs
(D) Professional fees directly related to acquisition

Ans :

(A) Subsequent costs on day-to-day servicing
The text under 'Measurement at recognition' makes a clear distinction between initial costs and later expenses. It explicitly states that "Subsequent costs on day-to-day servicing are not recognised as PPE." These are treated as revenue expenditures and are expensed to the Profit and Loss statement as they are incurred.

May/June 2021

99. How should an item of Property, Plant and Equipment acquired in exchange for a non-monetary asset generally be valued at recognition, according to AS-10?
(A) At the book value of the asset given up
(B) At the original cost of the asset given up
(C) At fair value
(D) At zero value, with a note in the accounts

Ans :

(C) At fair value

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or lives used
(B) The market value of all depreciable assets
(C) The names of the suppliers of the assets
(D) A forecast of future depreciation charges

Ans :

(A) The specific depreciation methods and rates or lives used
The source text from point 10 of the Ind AS 16 summary is direct and unambiguous. It mandates the disclosure of the "Depreciation methods used" (e.g., SLM, WDV) and the "Depreciation rates or the useful lives of the assets." This transparency allows users of financial statements to understand the company's depreciation policy.

May/June 2023

91. What is the primary purpose of Indian Accounting Standard (Ind AS) 38?
(A) To prescribe the accounting treatment for tangible assets
(B) To set rules for consolidating financial statements
(C) To govern the accounting for leases
(D) To deal with the accounting treatment for intangible assets

Ans :

(D) To deal with the accounting treatment for intangible assets
The annexure clearly introduces Ind AS 38 by stating, "This standard deals with accounting treatment for intangible assets." It specifies the criteria for recognizing and measuring these assets and the required disclosures, distinguishing it from Ind AS 16, which covers tangible assets (property, plant, and equipment).

Oct/Nov 2018

92. How does the guidance on amortisation methods in Ind AS 38 relate to the guidance on depreciation methods in Ind AS 16?
(A) The methods in Ind AS 38 are completely different from those in Ind AS 16.
(B) The methods and disclosures in Ind AS 38 are on lines similar to those in Ind AS 16.
(C) Ind AS 38 prohibits the use of methods like SLM and WDV.
(D) Ind AS 38 mandates only one specific method of amortisation.

Ans :

(B) The methods and disclosures in Ind AS 38 are on lines similar to those in Ind AS 16.
The chapter concludes its discussion on Ind AS 38 by stating, "The amortisation methods and disclosures are specified in this Standard on lines similar to those contained in Ind AS – 16, regarding depreciation." This indicates a consistent underlying principle for allocating the cost of both tangible and intangible long-term assets.

May/June 2007

93. Based on the summary of Ind AS 16, which of the following statements are correct?
1. Depreciable amount is defined as cost less residual value.
2. Depreciation is the systematic allocation of this amount over the asset's useful life.
3. Useful life must always be measured in terms of years.

(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2 and 3

Ans :

(A) 1 and 2 only
Statements 1 and 2 are correct definitions provided under Ind AS 16. Statement 3 is incorrect because the standard explicitly allows useful life to be measured either as a time period or as "the number of production or similar units expected to be obtained," not just in years.

Oct/Nov 2025

94. What is the stated objective of Accounting Standard AS-10?
(A) To prescribe the accounting for financial instruments
(B) To mandate the use of the Written Down Value method only
(C) To define the rules for business combinations
(D) To prescribe the accounting treatment for property, plant and equipment (PPE)

Ans :

(D) To prescribe the accounting treatment for property, plant and equipment (PPE)
The first sentence of the section on AS-10 in the annexure clearly states, "The objective of this Standard is to prescribe the accounting treatment for property, plant and equipment (PPE)." This establishes the scope and purpose of AS-10 as the

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(D) SLM, WDV & Units of Production method

The final point (i) in the summary of AS-10 depreciation rules provides a specific list of acceptable methods. It states, "Depreciation methods include SLM, WDV & Units of Production method." This confirms the recognition of these three primary methods under this accounting standard, consistent with the mention earlier in the chapter.

May/June 2014

105. **Assertion (A) :** The mere passage of time is sufficient to reduce an asset's value.

Reason (R) : An asset's value diminishes continuously even if it is not used, as exemplified by an old, unused car having negligible value years after its purchase.

(A) Both (A) and (R) are true and (R) is the correct explanation of (A)

(B) Both (A) and (R) are true but (R) is not the correct explanation of (A)

(C) (A) is true but (R) is false

(D) (A) is false but (R) is true

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A)

Assertion (A) states the principle of efflux of time. Reason (R) provides a clear example and elaboration of this principle, explaining that value diminishes even without use. The reason, therefore, directly illustrates and correctly explains the assertion, making both true and the reason a valid explanation of the assertion.

Oct/Nov 2007

106. Match the cause of depreciation in List-I with its correct description in List-II.

List-I (Cause)

P. Wear and Tear

Q. Efflux of Time

R. Obsolescence

S. Accidents

List-II (Description)

1. A new invention renders the asset useless.
2. An unforeseen event damages the asset.
3. The asset's value falls due to mere passage of time.
4. The asset deteriorates from actual use.

(A) P-4, Q-3, R-1, S-2

(B) P-3, Q-4, R-2, S-1

(C) P-4, Q-1, R-3, S-2

(D) P-2, Q-3, R-1, S-4

Ans :

(A) P-4, Q-3, R-1, S-2

The matching aligns with the definitions in the chapter: Wear and Tear (P) is deterioration from use (4). Efflux of Time (Q) is value loss from time passing (3). Obsolescence (R) is becoming outdated due to new inventions (1). Accidents (S) refer to unforeseen damaging events (2). This combination correctly pairs each cause with its description.

May/June 2025

107. Which of the following statements are correct regarding the need for depreciation?

1. To ascertain the correct profit or loss.
2. To show a true and fair financial position.
3. To make provision for the replacement of the asset.
4. To increase the market value of the asset.

(A) 1 and 2 only

(B) 1, 2 and 3 only

(C) 2, 3 and 4 only

(D) All of the above

Ans :

(B) 1, 2 and 3 only

The chapter lists three specific reasons for providing depreciation: (i) To know the correct profits, (ii) To show correct financial position, and (iii) To make provision for replacement of asset. Statement 4 is incorrect, as depreciation is an expense that reduces the book value of an asset, and does not increase its market value.

Oct/Nov 2019

108. A firm acquires a machine that is physically capable of running for 10 years. However, due to expected technological advancements, the firm plans to use it for only 8 years. What is the estimated useful life for depreciation calculation?

(A) 8 years

(B) 10 years

(C) 9 years

(D) The average of 8 and 10 years

Ans :

(A) 8 years

The chapter explicitly guides that for depreciation purposes, the firm should use the number of years the asset is likely to be used, not the number of years it can physically run. In this scenario,

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the economic life (8 years) is shorter than the physical life (10 years), so 8 years is the correct useful life.

May/June 2009

109. In the alternative method of recording depreciation, the 'Provision for Depreciation Account' is also known as a:
(A) Real Account
(B) Nominal Account
(C) Contra-Asset Account
(D) Suspense Account

Ans :

(C) Contra-Asset Account
The 'Provision for Depreciation Account' (or Accumulated Depreciation Account) is a contra-asset account. Its purpose is to hold a credit balance that reduces the gross value of a related asset account on the balance sheet. This allows the original cost of the asset to be preserved while still reporting its net book value.

Oct/Nov 2011

110. An asset is purchased for ₹1,50,000 with a scrap value of ₹10,000 and a useful life of 7 years. What is the annual depreciation charge under the Straight Line Method?
(A) ₹20,000
(B) ₹21,429
(C) ₹18,571
(D) ₹1,50,000

Ans :

(A) ₹20,000
Under the Straight Line Method, the annual depreciation is calculated using the formula:

$$= \frac{\text{Cost} - \text{Scrap Value}}{\text{Useful Life}}$$

Plugging in the values from the question, the calculation is

$$= \frac{1,50,000 - 10,000}{7 \text{ years}}$$

$$= \frac{1,40,000}{7} = 20,000 \text{ per year.}$$

May/June 2010

111. The Written Down Value method is considered more relevant for which of the following assets?
1. Vehicles
2. Computers
3. Office Equipment
4. Land

(A) 1 and 2 only
(B) 3 and 4 only
(C) All of the above
(D) 1, 2 and 3 only

Ans :

(D) 1, 2 and 3 only
The text explicitly mentions that the WDV method is more relevant for assets like "Vehicles, Computer, Office Equipment, etc." which provide better performance in their initial years. Land (4) is generally not depreciated, so it is excluded. Therefore, the first three assets are the correct choices from the list provided.

Oct/Nov 2024

112. What is the underlying rationale for the WDV method, where the depreciation amount is highest in the first year and gradually decreases?
(A) To simplify the calculation process over the asset's life.
(B) To match high initial depreciation with low initial repair costs.
(C) To comply with international tax laws only.
(D) To ensure the asset's book value matches its market value.

Ans :

(B) To match high initial depreciation with low initial repair costs.
The WDV method's declining charge is justified by the pattern of total asset-related costs. In the early years, depreciation is high, but repair costs are low. In later years, as repair costs rise, the depreciation charge falls. This creates a more stable, balanced total charge to the P&L account over the asset's life.

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May/June 2017

113. A mining company buys equipment for ₹50,00,000 with no scrap value. It is estimated to be able to extract 2,000,000 tonnes of ore over its life. In year one, 400,000 tonnes are extracted. Using the Units of Production method, calculate the depreciation for year one.
(A) ₹5,00,000
(B) ₹8,00,000
(C) ₹10,00,000
(D) ₹4,00,000

Ans :

(C) ₹10,00,000

First, calculate the depreciation rate per unit (tonne). The depreciable amount is ₹50,00,000 (cost - zero scrap value). The rate is

$$\frac{50,00,000}{2,000,000 \text{ tonnes}} = 2.5 \text{ per tonne}$$

For year one, the depreciation is the number of tonnes extracted multiplied by the rate:

$$400,000 \text{ tonnes} \times 2.5/\text{tonne} = 10,00,000$$

Oct/Nov 2005

114. Identify the incorrect pair regarding depreciation methods and their characteristics.

(A) Straight Line Method - Constant annual depreciation
(B) Written Down Value Method - Declining annual depreciation
(C) Units of Production Method - Usage-based depreciation
(D) Sum of the Years' Digits Method - Constant annual depreciation

Ans :

(D) Sum of the Years' Digits Method - Constant annual depreciation
The Sum of the Years' Digits (SYD) method is an accelerated depreciation method, meaning it results in a higher depreciation charge in the early years and a lower charge in the later years. It does not produce a constant annual depreciation amount; that is the characteristic of the Straight Line Method.

May/June 2020

115. What is the primary financial benefit of using an accelerated depreciation method like the Sum of the Years' Digits (SYD) method?

(A) It provides a greater tax benefit in the early years of an asset's life.
(B) It increases the total depreciation over the asset's life.
(C) It simplifies accounting and record-keeping.
(D) It makes the asset's book value equal to its market value.

Ans :

(A) It provides a greater tax benefit in the early years of an asset's life.
The chapter's description of the SYD method explicitly states that it "assumes a higher depreciation charge and a greater tax benefit in the early years of an asset's life." By front-loading the depreciation expense, taxable income is reduced more in the initial years, leading to a deferral of tax payments.

Oct/Nov 2015

116. The 'Sinking Fund' method for handling depreciation is specifically designed to facilitate what financial objective?

(A) Maximizing the annual profit reported
(B) Ensuring funds are available for asset replacement
(C) Paying for the day-to-day servicing of an asset
(D) Reducing the company's income tax liability

Ans :

(B) Ensuring funds are available for asset replacement
The Sinking Fund method goes beyond just accounting for depreciation as a non-cash expense. It involves actively setting aside cash and investing it, with the explicit goal of accumulating a fund that will be sufficient to purchase a new asset when the current one is retired, thereby planning for the cash outflow of replacement.

May/June 2013

117. Identify the correct statement(s) about amortisation.

1. It applies to intangible assets.
2. It is conceptually different from and unrelated to depreciation.
3. It is governed by Ind AS 38.

(A) 1 and 3 only
(B) 2 only
(C) 1, 2 and 3
(D) 1 and 2 only

Ans :

(A) 1 and 3 only
Statement 1 is correct; amortisation is for intangible assets. Statement 3 is also correct, as the chapter specifies that Ind AS 38 deals with intangible assets and their amortisation. Statement 2 is incorrect because the chapter states that amortisation is "similar to depreciation" and the discussion on depreciation is "equally applicable to amortization."

Oct/Nov 2021

118. The AICPA's description of depreciation accounting, as cited in the summary, emphasizes that it is a process of allocation, not a process of:

(A) Valuation

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(B) Estimation
(C) Verification
(D) Distribution

Ans :

(A) Valuation
The summary quotes the AICPA description, which concludes with the critical distinction: "It is the process of allocation and not of valuation." This highlights that depreciation's goal is to spread an asset's historical cost over its useful life, not to determine or report its current market value on the balance sheet.

May/June 2024

119. Identify the correct pair based on the concepts discussed in the chapter.
(A) Efflux of time - Value loss from new inventions
(B) Obsolescence - Value loss from physical usage
(C) Sinking Fund - Provision for asset replacement
(D) Amortisation - Depreciation of tangible assets

Ans :

(C) Sinking Fund - Provision for asset replacement
The Sinking Fund method is explicitly described as a way to set aside cash to ensure funds are available for replacing a fixed asset. The other pairs are incorrect: Efflux of time is value loss from time passage, obsolescence is from new inventions, and amortisation applies to intangible, not tangible, assets.

Oct/Nov 2008

120. **Assertion (A) :** As per Ind AS 16, each significant part of a Property, Plant, and Equipment (PPE) item must be depreciated separately.
Reason (R) : This component-based approach ensures the depreciation charge more accurately reflects the consumption pattern and useful life of each distinct part.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A)
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A)
(C) (A) is true but (R) is false
(D) (A) is false but (R) is true

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A)
Assertion (A) correctly states the rule of component depreciation from Ind AS 16. Reason (R) provides the correct underlying principle for this rule. Depreciating parts with different useful lives (like an aircraft engine and its body) separately leads to a more faithful representation of cost allocation. Thus, (R) correctly explains (A).

May/June 2006

121. Which of the following scenarios would justify a change in the depreciation method for an asset under Ind AS 16?
(A) A desire to report higher profits in the current year.
(B) A change in the entity's tax assessment.
(C) A significant change in how the asset is used, altering the pattern of economic benefits.
(D) The appointment of a new Chief Financial Officer.

Ans :

(C) A significant change in how the asset is used, altering the pattern of economic benefits.
Ind AS 16 allows a change in depreciation method only if there is "a change in the expected pattern of consumption of future economic benefits." A significant change in asset usage would alter this pattern, justifying a switch to a method that better reflects the new consumption pattern. The other options are not valid reasons.

Oct/Nov 2017

122. A company regularly incurs costs for oil changes and filter replacements for its fleet of delivery trucks. According to AS-10, how should these costs be treated?
(A) They should be capitalized and added to the cost of the trucks.
(B) They should be recognized as a revenue expense in the Statement of Profit and Loss.
(C) They should be deducted from the accumulated depreciation account.
(D) They should be ignored for accounting purposes.

Ans :

(B) They should be recognized as a revenue expense in the Statement of Profit and Loss.
AS-10 explicitly states that "Subsequent costs on day-to-day servicing are not recognised as

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PPE." These costs, like oil changes, are routine maintenance necessary to keep the asset running but do not enhance its original capability or extend its life. Therefore, they are expensed as incurred in the Profit and Loss statement.

May/June 2008

123. **Assertion (A) :** The depreciation method used for an asset must be reviewed at least at each financial year-end.
Reason (R) : This review ensures the chosen method continues to reflect the expected pattern of consumption of the asset's future economic benefits.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A)
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A)
(C) (A) is true but (R) is false
(D) (A) is false but (R) is true

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A)
AS-10 requires an annual review of the depreciation method (A). The reason for this review (R) is to ensure the accounting treatment remains appropriate. If the way an asset is used changes, the method might need to be updated to match the new pattern of benefit consumption. Thus, R correctly explains A.

Oct/Nov 2013

124. Match the cost item for a new machine (List-I) with its correct accounting treatment under AS-10 (List-II).
List-I (Cost Item)
P. Purchase price after trade discount
Q. Import duties (non-refundable)
R. Cost of day-to-day servicing
S. Cost of dismantling the asset at end of life
List-II (Accounting Treatment)
1. Capitalized as part of PPE cost
2. Recognized as an expense when incurred
(A) P-1, Q-1, R-2, S-1
(B) P-2, Q-2, R-1, S-2
(C) P-1, Q-2, R-1, S-2
(D) P-1, Q-1, R-1, S-2

Ans :

(A) P-1, Q-1, R-2, S-1
Under AS-10, the purchase price (P), non-refundable taxes like import duties (Q), and estimated dismantling costs (S) are all capitalized as part of the asset's cost. However, day-to-day servicing costs (R) are treated as revenue expenditure and expensed in the P&L statement as they occur. This aligns with the matching P-1, Q-1, R-2, S-1.

May/June 2015

125. Consider the following costs incurred for a new machine:
1. Purchase price
2. Non-refundable import duties
3. Trade discount received
4. Cost of dismantling the old machine being replaced
Which of these items are included in the cost of the new PPE as per AS-10?
(A) 1 and 2 only
(B) 1, 2 and 4 only
(C) 1 and 2 after deducting 3
(D) 1, 2, 3 and 4

Ans :

(C) 1 and 2 after deducting 3
AS-10 states the cost includes purchase costs after adjusting for trade discounts/rebates, and non-refundable taxes. Therefore, the purchase price (1) and import duties (2) are included, but the trade discount (3) must be deducted. The cost of dismantling a previous machine is not a cost of the new asset.

Oct/Nov 2012

126. Which statement correctly distinguishes between Amortisation and Depreciation?
(A) Amortisation is for tangible assets, while depreciation is for intangible assets.
(B) Amortisation is for intangible assets, while depreciation is for tangible assets.
(C) Amortisation is a cash expense, while depreciation is a non-cash expense.
(D) Amortisation uses the WDV method, while depreciation uses the SLM method.

Ans :

(B) Amortisation is for intangible assets, while depreciation is for tangible assets.
The chapter makes a clear distinction between the two terms. Depreciation is the process of allocating the cost of tangible assets (like machinery, buildings) over their useful life. Amortisation is the equivalent process for intangible assets (like patents, copyrights), which

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The standard specifies the accounting treatment for asset exchanges. It states that "PPE acquired in exchange for a non-monetary asset or assets... are to be valued at fair value barring some exceptions." This ensures the new asset is recorded at its current market-based value at the time of the transaction.

Oct/Nov 2010

100. What does AS-10 mandate regarding the depreciation of an asset that has multiple parts with significant individual costs?
(A) The entire asset must be depreciated using a single composite rate.
(B) Only the most expensive part should be depreciated.
(C) Depreciation is not required for such complex assets.
(D) Each part with a significant cost should be depreciated separately.

Ans :

(D) Each part with a significant cost should be depreciated separately.
Point (a) under the 'Depreciation' section of the AS-10 summary is identical to the rule in Ind AS 16. It states that "Each part of an item of PPE with a cost that is significant in relation to the total cost of the item should be depreciated separately." This is known as component accounting.

May/June 2005

101. Based on this rule from the AS-10 summary, what is the required frequency for reviewing the estimates of an asset's residual value and useful life?
"(d) Residual value & useful life to be reviewed at each balance sheet date."
(A) At least at each financial year end
(B) Only when the asset is acquired
(C) Every five years
(D) Only if the asset is damaged

Ans :

(A) At least at each financial year end
The source text explicitly states that the residual value and useful life are "to be reviewed at each balance sheet date." Since the balance sheet is prepared at the end of each financial period (typically annually), this rule mandates a review at least at each financial year-end to ensure the estimates remain appropriate.

Oct/Nov 2022

102. Under AS-10, if an entity changes its method of depreciation for an asset, how is this change accounted for?
(A) As a prior period error
(B) As a change in an accounting estimate as per AS 5
(C) As a change in accounting policy with retrospective effect
(D) It is not permitted to change the depreciation method

Ans :

(B) As a change in an accounting estimate as per AS 5
The annexure, in point (h) under the AS-10 depreciation rules, specifies that "Any change is accounted for as change in an accounting estimate as per AS 5." This means the effect of the change is applied prospectively (to the current and future periods) rather than by restating prior periods.

May/June 2018

103. The depreciation method used should reflect the pattern in which the asset's future economic benefits are expected to be _____ by the enterprise.
(A) Sold
(B) Repaired
(C) Consumed
(D) Insured

Ans :

(C) Consumed
Point (f) of the AS-10 depreciation rules states that the "Depreciation method used should reflect the pattern in which the asset's future economic benefits are expected to be consumed by the enterprise." This principle requires a firm to choose the method (SLM, WDV, etc.) that best matches how the asset's value is used up.

Oct/Nov 2016

104. Which three depreciation methods are explicitly mentioned as being included under the provisions of AS-10?
(A) SLM, WDV & Annuity method
(B) SLM, WDV & Sinking Fund method
(C) WDV, Units of Production & Annuity method
(D) SLM, WDV & Units of Production method

Ans :

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CHAPTER 7

Capital and Revenue Expenditure

Oct/Nov 2015

1. According to the typical structure of final accounts, where are expenses and receipts of a revenue nature generally shown?

(A) In the Cash Flow Statement under operating activities

(B) In the Trading and Profit and Loss Account

(C) In a separate statement of revenue items appended to the Balance Sheet

(D) In the Balance Sheet as assets and liabilities

Ans :

(B) In the Trading and Profit and Loss Account

At the end of an accounting year, final accounts are prepared from the trial balance. All balances of a revenue nature, including expenses and receipts, are transferred to the Trading and Profit and Loss Account to determine the net profit or loss for the period. Capital items are taken to the balance sheet.

May/June 2024

2. Where are expenses and receipts of a capital nature primarily recorded in the final accounts of a business?

(A) In the Balance Sheet

(B) In the Trading Account

(C) In the Profit and Loss Account

(D) In the Trial Balance only

Ans :

(A) In the Balance Sheet

Expenses and receipts that are capital in nature, such as the purchase of fixed assets or raising capital through share issuance, are taken to the Balance Sheet. These items affect the financial position of the entity over multiple accounting periods and are not used for calculating the profit for the current period.

Oct/Nov 2008

3. Which of the following is one of the primary factors considered when deciding whether an expenditure is 'capital' or 'revenue'?

(A) The timing of the payment, such as being paid in advance or in arrears

(B) The geographical location of the expenditure, for instance, domestic or international

(C) The nature of the expense, specifically whether it is recurring or non-recurring

(D) The method of payment for the transaction, for example, using cash or credit

Ans :

(C) The nature of the expense, specifically whether it is recurring or non-recurring

The classification of an expenditure as capital or revenue depends on several factors. One of the most common tests is the nature of the expense. This involves assessing whether the transaction is recurring, meaning it occurs frequently in the normal course of business, or if it is a non-recurring, one-time expenditure.

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May/June 2006

4. An expenditure is classified as capital or revenue based on which of the following set of factors?

(A) Amount of the expense, Method of payment, and Approval authority for the transaction

(B) Frequency of payment, Tax implications of the expense, and Supplier's classification

(C) Market value of the item, Depreciation method chosen, and the Source of funds used

(D) Nature of the expense, Effect on revenue earning capacity, and Benefit from the expenditure

Ans :

(D) Nature of the expense, Effect on revenue earning capacity, and Benefit from the expenditure

The determination of an expenditure as capital or revenue is not based on a single rule but on a combination of factors. The three key considerations are the nature of the expense (recurring/non-recurring), its effect on the business's revenue-earning capacity, and the duration of the benefit derived from the expenditure (short-term or long-term).

Revenue receipts represent the income earned by the business during an accounting period. To determine the net profit or loss, these receipts are credited to the Trading and Profit & Loss Account, where they are matched against the revenue expenses incurred during the same period. This is a fundamental aspect of accrual accounting.

May/June 2024

44. A grant received from the government for the purpose of building a new factory is an example of a:
(A) Deferred Income
(B) Operational Subsidy
(C) Revenue Receipt
(D) Capital Receipt

Ans :

(D) Capital Receipt
Government grants are classified based on their purpose. A grant received specifically for the construction or acquisition of a capital asset, such as a factory, is treated as a capital receipt. It is not considered revenue from ordinary operations. Its accounting treatment often involves either reducing the cost of the asset or setting it up as deferred income.

Oct/Nov 2008

45. Which of the following is an example of a revenue receipt?
(A) Sales of goods on credit
(B) Sale of old machinery
(C) Money obtained from issuing debentures
(D) Loan taken from a bank

Ans :

(A) Sales of goods on credit
Sales of goods, whether for cash or on credit, are the primary operating activity for most businesses and represent revenue earned. This is a classic example of a revenue receipt. The other options—sale of machinery (capital receipt), issuing debentures (capital receipt), and a bank loan (liability)—are not generated from day-to-day operations.

May/June 2006

46. What type of expenditure generates enduring benefits and helps in revenue generation over more than one accounting period?
(A) Deferred Revenue Expenditure
(B) Capital Expenditure
(C) Operational Expenditure
(D) Revenue Expenditure

Ans :

(B) Capital Expenditure
Capital expenditure is defined by its long-term impact. It is an investment in assets that generate enduring benefits, contributing to the business's revenue-generating activities for multiple accounting periods. This long-term benefit profile is what distinguishes it from revenue expenditure, whose benefits are consumed within a single period.

Oct/Nov 2017

47. Receipts that arise in the ordinary course of business are known as:
(A) Capital receipts
(B) Non-recurring receipts
(C) Revenue receipts
(D) Financial receipts

Ans :

(C) Revenue receipts
Revenue receipts are inflows of cash or other assets that arise from the main, day-to-day activities of an enterprise. These are the regular and recurring incomes of the business, such as revenue from sales, service fees, interest, and royalties. They are central to measuring a company's operational performance in the Profit & Loss Account.

May/June 2008

48. Consider the following two statements:
Statement I : The purpose of revenue expenditure is to maintain fixed assets in good working condition.
Statement II : The purpose of capital expenditure is to improve or enhance the earning capacity of the business.
(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Only Statement I is correct.
(D) Only Statement II is correct.

Ans :

(A) Both Statement I and Statement II are correct.
Both statements accurately describe the fundamental purposes of the two types of expenditure. Revenue expenditure is for maintenance and day-to-day operations,

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(A) Over more than one accounting period
(B) Only in the current accounting period
(C) Only in the subsequent accounting period
(D) Retroactively for past accounting periods

Ans :

(A) Over more than one accounting period
An expenditure is classified as capital if it helps the business generate revenue over multiple accounting periods. The purchase of a plant is a classic example, as the asset is expected to be used in production for several years, contributing to revenue generation throughout its useful life. This long-term benefit distinguishes it from revenue expenditure.

Oct/Nov 2020

11. An expenditure is considered a revenue expenditure if the benefit derived from it is of what duration?
(A) Of long duration, spanning several years
(B) Indefinite duration
(C) A duration of exactly three years
(D) Of short duration, typically within one accounting period

Ans :

(D) Of short duration, typically within one accounting period
The duration of the benefit is a key criterion for classifying expenditure. If the benefit from an incurred expense is consumed or exhausted within the current accounting period, it is considered a revenue expenditure. This contrasts with capital expenditure, where the benefit extends over a long duration, covering multiple accounting years.

May/June 2022

12. What is the main purpose of incurring a capital expenditure, in terms of its benefit?
(A) To meet routine operational needs and settle monthly expenses for the business
(B) To earn income over multiple years or increase the business's long-term earning capacity
(C) To reduce the current year's taxable income by maximizing deductible expenses
(D) To settle short-term liabilities and improve the company's current liquidity ratio

Ans :

(B) To earn income over multiple years or increase the business's long-term earning capacity
Capital expenditure is undertaken with the primary objective of acquiring assets that will provide long-term benefits. The main purpose is to either enhance the business's earning capacity or to generate income over several future accounting periods. This long-term perspective on benefit and income generation is a defining characteristic of capital expenditure.

Oct/Nov 2023

13. Which of the following statements correctly defines capital expenditure?
(A) It is an expenditure whose benefits are fully utilized within the current accounting year.
(B) It is a recurring expenditure incurred to maintain the daily operations of the business.
(C) It is an expenditure whose benefit is consumed over multiple years, not just one.
(D) It is an expenditure that is consistently small in value and occurs frequently in business.

Ans :

(C) It is an expenditure whose benefit is consumed over multiple years, not just one.
Capital expenditure is fundamentally defined by the longevity of its benefits. It is an outlay of funds that results in the acquisition of an asset or an improvement to an existing asset, where the associated economic benefits are expected to be realized by the business over multiple accounting periods, not just the current one.

May/June 2016

14. Which of the following is an example of capital expenditure?
(A) Salaries paid to administrative staff
(B) Electricity bill for the factory
(C) Annual maintenance contract for office computers
(D) Purchase of patent rights for a new technology

Ans :

(D) Purchase of patent rights for a new technology
The purchase of patent rights is a capital expenditure because it involves acquiring an intangible asset that provides exclusive rights and economic benefits to the business for many years. The other options—maintenance contracts, salaries, and electricity bills—are all recurring operational costs whose benefits are consumed

Oct/Nov 2017

5. How are recurring expenditures, such as the payment of salaries, rent, and telephone charges, typically classified in accounting?
(A) As deferred revenue expenditures
(B) As prepaid expenditures
(C) As revenue expenditures
(D) As capital expenditures

Ans :

(C) As revenue expenditures
Recurring expenditures are those that occur frequently and are related to the day-to-day operations of a business. Examples include salaries, rent, and purchase of raw materials. Since these expenses are consumed within the current accounting period to generate revenue, they are classified as revenue expenditures and charged to the Profit and Loss Account.

May/June 2008

6. A non-recurring expenditure is generally considered to be of what nature?
(A) Always revenue in nature regardless of the amount
(B) Capital in nature, subject to the materiality concept
(C) Always deferred revenue in nature for future amortization
(D) A contingent liability recorded in the notes to accounts

Ans :

(B) Capital in nature, subject to the materiality concept
A non-recurring expenditure, which does not happen frequently, is typically capital in nature as it often involves the acquisition of a long-term asset. However, this is subject to the materiality concept. If a non-recurring expense is of a very small amount, it may be treated as a revenue expense for convenience.

Oct/Nov 2013

7. A company purchases a wall clock for ₹500. Although this is a non-recurring expenditure, it is treated as a revenue expense. This treatment is based on which accounting concept?
(A) The Business Entity Concept
(B) The Going Concern Concept
(C) The Dual Aspect Concept
(D) The Materiality Concept

Ans :

(D) The Materiality Concept
The materiality concept states that items of small value, which are technically capital in nature, can be treated as revenue expenses. The purchase of a wall clock for ₹500 is non-recurring, but its value is insignificant in the context of the overall financial statements. Therefore, it is expensed immediately rather than capitalized and depreciated.

May/June 2015

8. Which of the following is an example of a capital expenditure based on the 'nature of expense' test?
(A) Purchase of a motor car for the business
(B) Payment of monthly office rent
(C) Purchase of raw materials for production
(D) Payment of annual insurance premium

Ans :

(A) Purchase of a motor car for the business
Based on the nature of the expense, recurring items are revenue, while non-recurring items are generally capital. The purchase of a motor car is a non-recurring event that provides long-term benefits to the business. In contrast, rent, raw materials, and insurance premiums are recurring expenses incurred for day-to-day operations, making them revenue expenditures.

Oct/Nov 2012

9. If an expenditure helps to generate revenue only in the current accounting period, how is it classified?
(A) Deferred Revenue Expenditure
(B) Capitalized Revenue Expenditure
(C) Revenue Expenditure
(D) Capital Expenditure

Ans :

(C) Revenue Expenditure
Expenses that help generate income or revenue within the current year are considered revenue in nature. According to the matching principle, these costs should be matched against the revenue they help to earn in the same period. Therefore, they are treated as revenue expenditures and debited to the Profit and Loss account.

May/June 2011

10. The purchase of a new plant is generally called a 'Capital Expenditure' because it helps to generate revenue over what period?

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The costs of replacing parts of an asset at regular intervals are treated as capital expenditure because they enhance or restore the future economic benefits of the asset. This is distinct from day-to-day maintenance, which is a revenue expense.

May/June 2012

20. The costs of major inspections for potential faults in an asset are classified as:
(A) A deferred revenue expenditure, requiring write-off over a fixed period of 3 years
(B) Revenue expenditure, since they are considered a form of preventive or routine maintenance
(C) A provision for future repairs, which is recorded on the balance sheet as a liability
(D) Capital expenditure, as performing them is a condition for the asset's continued operation

Ans :

(D) Capital expenditure, as performing them is a condition for the asset's continued operation
The cost of a major inspection for faults is capitalized as a subsequent cost. This is because performing such inspections is often a necessary condition for the continued operation of the asset, and the expenditure provides benefits over a period until the next inspection. It is treated as a replacement of a component of the asset.

Oct/Nov 2014

21. Which of the following costs incurred for an asset would be classified as a capital expenditure?
(A) Cost of small parts used in routine maintenance
(B) Annual insurance premium for the asset
(C) Costs of site preparation for installing the asset
(D) Costs of day-to-day servicing of the asset

Ans :

(C) Costs of site preparation for installing the asset
Costs of site preparation are directly attributable to bringing an asset to the location and condition necessary for it to be operational. Therefore, they are included in the initial cost of the asset and are classified as capital expenditure. The other options represent routine operational expenses, which are treated as revenue expenditures.

May/June 2019

22. How are initial delivery and handling costs for a newly purchased machine treated?
(A) As a deferred revenue expenditure
(B) As a capital expenditure, added to the cost of the machine
(C) As a general administrative overhead
(D) As a revenue expenditure in the period incurred

Ans :

(B) As a capital expenditure, added to the cost of the machine
Initial delivery and handling costs are directly related to bringing the asset to the location required for its operation. According to accounting standards, such directly attributable costs are part of the initial cost of the asset. Therefore, they are capitalized by adding them to the purchase price of the machine, not expensed immediately.

Oct/Nov 2006

23. A company pays professional fees to an architect for designing its new factory building. This expenditure is:
(A) An administrative overhead
(B) A deferred revenue expenditure
(C) A capital expenditure
(D) A revenue expenditure

Ans :

(C) A capital expenditure
Professional fees, such as those paid to architects or engineers for the construction or acquisition of a fixed asset, are considered directly attributable costs. Since these fees are essential for bringing the asset into existence and making it ready for use, they are capitalized as part of the cost of that asset (the factory building).

May/June 2021

24. Which of the following statements regarding expenditure classification is correct?
(A) All research expenditure is consistently classified as a form of capital expenditure
(B) Installation and assembly costs for a new plant are always treated as revenue expenditure
(C) The costs associated with testing a new asset are always treated as revenue expenditure
(D) Employee benefit costs arising directly from an asset's construction are a capital

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expenditure

Ans :

(D) Employee benefit costs arising directly from an asset's construction are a capital expenditure
Costs that are directly attributable to the construction or acquisition of an asset are capitalized. This includes employee benefit costs (like wages) for workers directly involved in constructing the asset. Costs of testing and installation are also capitalized. However, research expenditure is generally treated as revenue, while certain development expenditures might be capitalized.

Oct/Nov 2010

25. How should a company classify the costs of day-to-day servicing of its tangible and intangible assets?
(A) As a long-term liability
(B) As a reduction from the asset's value
(C) As revenue expenditure
(D) As capital expenditure

Ans :

(C) As revenue expenditure
The costs of day-to-day servicing, which primarily include labor, consumables, and small parts, are incurred to maintain the asset in its current working condition. These expenses do not enhance the asset's earning capacity or extend its life; they merely maintain it. Therefore, they are treated as revenue expenditure and expensed in the period incurred.

May/June 2005

26. A bank incurs costs to open a new branch in a new city. How are these costs, such as for market research and initial promotion, classified?
(A) As an intangible asset
(B) As revenue expenditure
(C) As a deferred revenue expenditure
(D) As capital expenditure, part of the branch building cost

Ans :

(B) As revenue expenditure
The costs of opening a new facility, introducing a new product or service, or conducting business in a new location are treated as revenue expenditure. These include administrative and other general costs that are not directly tied to the acquisition of a specific long-term asset. They are considered operational start-up costs and are expensed as incurred.

Oct/Nov 2022

27. If a company incurs costs to reorganize part of its operations by moving a department to a different floor, how is this expenditure treated?
(A) As a prior period adjustment
(B) As a capital expenditure
(C) As an increase in the value of the building
(D) As a revenue expenditure

Ans :

(D) As a revenue expenditure
The costs associated with relocating or reorganizing part or all of an entity's operations are not capitalized. These costs do not result in the acquisition of a new asset or a significant enhancement of an existing one. Instead, they are considered operational expenses related to improving efficiency or changing structure and are treated as revenue expenditure.

May/June 2018

28. Expenditure on training staff to operate a newly acquired asset is classified as:
(A) Revenue expenditure.
(B) Capital expenditure, as it is related to the new asset.
(C) A part of the cost of the new asset.
(D) A deferred cost to be amortized over the asset's life.

Ans :

(A) Revenue expenditure.
Although the training is necessitated by the acquisition of a new asset, the expenditure on training staff is not capitalized. This cost relates to making the workforce ready to use the asset and is considered an operating expense. Accounting standards classify such staff training costs as revenue expenditure, to be expensed as incurred.

Oct/Nov 2016

29. How are costs incurred to generate internal goodwill, brands, and mastheads treated in accounting?
(A) They are capitalized only if a ready market exists for them.
(B) They are set aside in a special reserve account.
(C) They are treated as revenue expenditure.
(D) They are always capitalized as intangible assets.

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Ans :

(C) They are treated as revenue expenditure.
Costs on internally generated assets like goodwill, brands, mastheads, publishing titles, and customer lists are not capitalized. These expenditures, such as advertising and promotional activities, cannot be reliably measured and distinguished from the cost of developing the business as a whole. Therefore, they are recognized as revenue expenditure when they are incurred.

May/June 2014

30. Which of the following costs is NOT classified as a capital expenditure?
(A) Costs of relocating an entity's operations
(B) Installation and assembly costs of a machine
(C) Purchase price of a computer software
(D) Professional fees for acquiring a building

Ans :

(A) Costs of relocating an entity's operations
Costs incurred for relocating or reorganizing part or all of an entity's operations are treated as revenue expenditure. They are expensed in the period they are incurred. In contrast, the purchase price of software, installation costs, and professional fees for asset acquisition are all directly related to acquiring and preparing a long-term asset for use and are capitalized.

Oct/Nov 2007

31. When a fixed asset is acquired by paying a cheque, which account is debited in the books of the business entity?
(A) The Bank account
(B) The Cash account
(C) The Purchases account
(D) The Asset account

Ans :

(D) The Asset account
According to the rules of accounting, when an asset is acquired, the asset account is debited to record the increase in assets. Since the payment is made by cheque, the bank balance decreases, and therefore the bank account is credited. The journal entry is Debit Asset Account and Credit Bank Account, reflecting the acquisition.

May/June 2025

32. Company ABC Ltd purchases computer software for its designing business for ₹200,000 and pays by cheque. What is the correct accounting entry in the books of ABC Ltd?
(A) Dr Purchases account ₹200,000; Cr Bank account ₹200,000
(B) Dr Asset (Software) account ₹200,000; Cr Bank account ₹200,000
(C) Dr P&L account ₹200,000; Cr Bank account ₹200,000
(D) Dr Bank account ₹200,000; Cr Asset (Software) account ₹200,000

Ans :

(B) Dr Asset (Software) account ₹200,000; Cr Bank account ₹200,000
The purchase of computer software is a capital expenditure as it is an intangible asset providing long-term benefits. The correct entry is to debit the asset account to record its acquisition and credit the bank account to reflect the payment made via cheque. This correctly increases the company's assets and decreases its bank balance.

Oct/Nov 2019

33. Which of the following statements accurately describes a key distinction between capital and revenue expenditure?
(A) Capital expenditure appears in the profit and loss account; revenue expenditure appears in the balance sheet.
(B) Capital expenditure is a recurring cost for operations; revenue expenditure is a non-recurring cost.
(C) Capital expenditure provides a long-duration benefit; revenue expenditure provides a short-duration benefit.
(D) Capital expenditure involves a small amount of money; revenue expenditure involves a large amount.

Ans :

(C) Capital expenditure provides a long-duration benefit; revenue expenditure provides a short-duration benefit.
A primary distinguishing factor is the duration of the benefit. Capital expenditure provides benefits that extend over multiple accounting periods (long duration). In contrast, the benefits of revenue expenditure are typically consumed within a single accounting period (short duration). This difference in the timeline of benefits dictates their accounting treatment and presentation in financial statements.

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within the current period, making them revenue expenditures.

Oct/Nov 2009

15. Capital expenditure relates to which type of assets?
(A) Both tangible fixed assets and intangible assets
(B) Only tangible fixed assets like buildings and machinery
(C) Only current assets like inventory and receivables
(D) Only intangible assets like goodwill and trademarks

Ans :

(A) Both tangible fixed assets and intangible assets
The concept of capital expenditure is not limited to physical assets. It applies to any expenditure that creates a long-term advantage. This includes both tangible fixed assets, such as property, plant, and equipment, and intangible assets, such as computer software, patents, and copyrights, which provide benefits over multiple accounting periods.

May/June 2023

16. Which Indian Accounting Standard (Ind AS) specifically deals with the accounting for tangible fixed assets like property, plant, and equipment?
(A) Ind AS 38
(B) Ind AS 16
(C) Ind AS 2
(D) Ind AS 10

Ans :

(B) Ind AS 16
Indian Accounting Standard (Ind AS) 16, titled 'Property, Plant and Equipment', prescribes the accounting treatment for tangible fixed assets. It covers aspects like recognition, measurement of cost, subsequent measurement, and depreciation. This standard helps in correctly classifying costs related to these assets as capital or revenue, ensuring proper financial reporting.

Oct/Nov 2018

17. The accounting treatment for intangible assets is governed by which Indian Accounting Standard (Ind AS)?
(A) Ind AS 16
(B) Ind AS 38
(C) Ind AS 1
(D) Ind AS 24

Ans :

(B) Ind AS 38
Indian Accounting Standard (Ind AS) 38, titled 'Intangible Assets', provides guidance on the recognition, measurement, and disclosure of intangible assets. It helps entities decide which costs associated with items like software, patents, and brands should be capitalized and which should be expensed, thereby distinguishing between capital and revenue expenditure for non-physical assets.

May/June 2007

18. What do the initial costs of an asset, which are classified as capital expenditure, typically include?
(A) Purchase price, non-refundable taxes, and other directly attributable costs
(B) Only the initial purchase price of the asset, excluding all taxes or delivery fees
(C) Only the costs for bringing the asset to its location, excluding the purchase price
(D) Only non-refundable taxes and installation fees, excluding the initial purchase price

Ans :

(A) Purchase price, non-refundable taxes, and other directly attributable costs
The initial cost of an asset to be capitalized includes all expenditures necessary to acquire it and make it ready for its intended use. This comprises the basic purchase price, any import duties and non-refundable purchase taxes, and any costs directly attributable to bringing the asset to the location and condition necessary for it to be operational.

Oct/Nov 2025

19. Subsequent costs, such as the replacement of parts of an asset at regular intervals, are treated as what type of expenditure?
(A) Revenue expenditure
(B) Deferred revenue expenditure
(C) Capital expenditure
(D) Contingent expenditure

Ans :

(C) Capital expenditure
Subsequent costs incurred on an asset are capitalized if they meet the recognition criteria.

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A capital receipt is a receipt of money that is not from the ordinary course of business operations and typically creates a liability or reduces an asset. Funds received from the issuance of equity or preference shares represent an inflow of capital from owners, creating an obligation (in the form of equity), and are therefore classified as capital receipts.

Oct/Nov 2005

39. How is the amount received from the sale or disposal of a fixed asset, such as machinery, classified?

(A) As an extraordinary income
(B) As a miscellaneous income
(C) As a capital receipt
(D) As a revenue receipt

Ans :

(C) As a capital receipt
The amount received from the sale of a fixed asset is a capital receipt. This transaction is not part of the regular, day-to-day operating activities of the business. It involves the disposal of a long-term asset. While the total sale proceeds are a capital receipt, any resulting profit or loss is a revenue item.

May/June 2020

40. Are capital receipts routed through the Profit & Loss account?

(A) No, capital receipts are not routed through the Profit & Loss account.
(B) Yes, they are always shown as income in the P&L account.
(C) Only if the receipt is in cash and not by cheque.
(D) Yes, but only the portion exceeding the book value of the asset.

Ans :

(A) No, capital receipts are not routed through the Profit & Loss account.
Capital receipts, such as funds from share issuance or the sale of fixed assets, are not considered revenue for the period. Therefore, they are not credited to the Profit & Loss account. Instead, they are directly reflected on the Balance Sheet, for instance, by increasing cash and share capital or by reducing the value of fixed assets.

Oct/Nov 2015

41. When a fixed asset is sold, how is the profit or loss on the transaction recorded?

(A) It is adjusted directly against the capital account.
(B) It is treated as a capital receipt and shown in the Balance Sheet.
(C) It is ignored in the financial statements.
(D) It is recorded in the Profit & Loss account.

Ans :

(D) It is recorded in the Profit & Loss account.
While the total proceeds from the sale of a fixed asset are a capital receipt, the gain or loss arising from the transaction is revenue in nature. The profit (if sale price exceeds book value) or loss (if sale price is less than book value) is calculated and must be recognized in the Profit & Loss account for the period.

May/June 2013

42. What are revenue receipts?

(A) Receipts from the sale of fixed assets.
(B) Receipts from the day-to-day operations of the company.
(C) Receipts from the issuance of long-term loans.
(D) Grants received from the government for building capital assets.

Ans :

(B) Receipts from the day-to-day operations of the company.
Revenue receipts are the primary source of income for a business, generated from its main operating activities. Examples include sales of goods, fees for services rendered, interest, and dividends received. These receipts are recurring in nature and are fundamental to calculating the profitability of the business for an accounting period.

Oct/Nov 2021

43. Through which financial statement are revenue receipts routed?

(A) The Statement of Changes in Equity
(B) The Cash Flow Statement only
(C) The Profit & Loss Account
(D) The Balance Sheet

Ans :

(C) The Profit & Loss Account

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May/June 2009

34. What is the typical purpose of incurring a revenue expenditure?
(A) To issue new equity shares to raise funds
(B) To improve or enhance the earning capacity of the business
(C) To acquire a new long-term asset
(D) To maintain the fixed assets in good working condition

Ans :

(D) To maintain the fixed assets in good working condition
Revenue expenditure is incurred for the day-to-day running of the business and to maintain the existing earning capacity. This includes costs like repairs and maintenance, which are necessary to keep fixed assets in good working order but do not enhance their capacity or significantly extend their useful life. Such costs are expensed immediately.

Oct/Nov 2011

35. How are capital and revenue expenditures presented in the final financial statements?
(A) Capital expenditure is in the balance sheet; revenue expenditure is in the profit and loss account.
(B) Both capital and revenue expenditures are presented together only in the balance sheet.
(C) Both capital and revenue expenditures are presented together only in the profit and loss account.
(D) Capital expenditure is in the profit and loss account; revenue expenditure is in the balance sheet.

Ans :

(A) Capital expenditure is in the balance sheet; revenue expenditure is in the profit and loss account.
Capital expenditure results in the creation of an asset, which is reported on the balance sheet. Its cost is gradually recognized as an expense (depreciation) over its useful life. Revenue expenditure, on the other hand, is fully expensed in the period it is incurred and is therefore shown in the profit and loss account.

May/June 2010

36. Identify the incorrect statement regarding the distinction between capital and revenue expenditure.
(A) The benefit from revenue expenditure is of short duration.
(B) The purpose of revenue expenditure is to enhance the productive capacity of the business.
(C) Capital expenditure is non-recurring in nature.
(D) The amount spent on capital expenditure is usually large.

Ans :

(B) The purpose of revenue expenditure is to enhance the productive capacity of the business.
The purpose of revenue expenditure is to maintain the existing productive capacity and support day-to-day operations, not to enhance it. The purpose of improving or enhancing the business's productive or earning capacity is a characteristic of capital expenditure. The other statements accurately describe the differences between the two types of expenditures.

Oct/Nov 2024

37. Which of the following is a characteristic of capital expenditure?
(A) It is shown in the profit and loss account.
(B) The amount spent is relatively small.
(C) The purpose is to improve or enhance business earning capacity.
(D) It is recurring in nature.

Ans :

(C) The purpose is to improve or enhance business earning capacity.
A defining characteristic of capital expenditure is its purpose. It is incurred not just to maintain operations but to improve the business's structure or enhance its earning capacity for the long term. This contrasts with revenue expenditure, which is aimed at maintaining the current level of operations and profitability within a short period.

May/June 2017

38. A receipt from the issue of Equity or Preference shares is an example of what type of receipt?
(A) Capital Receipt
(B) Revenue Receipt
(C) Deferred Revenue Receipt
(D) Operational Receipt

Ans :

(A) Capital Receipt

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preserving the current earning capacity. Capital expenditure is for acquisition or significant improvement of assets, aimed at enhancing or increasing the earning capacity of the business over the long term.

Oct/Nov 2013

49. Consider the following statements:
Assertion (A): The purchase of a large, expensive machine is treated as a capital expenditure.
Reason (R) : The benefit from the machine is expected to last for a long duration, and the expenditure is non-recurring.
(A) Both A and R are true, and R is the correct explanation of A.
(B) Both A and R are true, but R is not the correct explanation of A.
(C) A is true, but R is false.
(D) A is false, but R is true.

Ans :

(A) Both A and R are true, and R is the correct explanation of A.
The assertion that purchasing an expensive machine is a capital expenditure is correct. The reason provides the justification: such an expenditure is non-recurring and provides long-term benefits, which are the key criteria for classifying an item as capital expenditure. Therefore, the reason correctly explains the assertion.

May/June 2015

50. Which of the following pairs is incorrectly matched?
(A) Legal fees to acquire property : Revenue Expenditure
(B) Purchase of raw materials : Revenue Expenditure
(C) Sale of goods : Revenue Receipt
(D) Issue of shares : Capital Receipt

Ans :

(A) Legal fees to acquire property : Revenue Expenditure
Legal fees paid to acquire a property are a directly attributable cost necessary to complete the acquisition of a long-term asset. Therefore, these fees should be capitalized along with the cost of the property, making them a capital expenditure. The other pairs correctly match the transaction type with its classification.

Oct/Nov 2012

51. Which of the following is NOT a revenue expenditure?
(A) Cost of building an extension to the factory
(B) Salaries paid to employees
(C) Cost of goods sold
(D) Office rent

Ans :

(A) Cost of building an extension to the factory
The cost of building an extension to the factory results in an enhancement of the existing asset, increasing its capacity and future economic benefits. This is a classic example of a capital expenditure. Salaries, cost of goods sold, and rent are all operational costs whose benefits are consumed within the period, making them revenue expenditures.

May/June 2011

52. Identify the correct statement from the following.
(A) Capital expenditure is always of a small amount.
(B) Revenue expenditure is non-recurring in nature.
(C) Capital receipts are recorded in the Profit & Loss Account.
(D) Profit on the sale of a fixed asset is a revenue receipt.

Ans :

(D) Profit on the sale of a fixed asset is a revenue receipt.
While the sale proceeds of a fixed asset are a capital receipt, the resulting profit (or loss) is considered revenue in nature and is reported in the Profit & Loss account. The other statements are incorrect: capital expenditure is usually large, revenue expenditure is recurring, and capital receipts are shown on the balance sheet.

Oct/Nov 2020

53. A company spends a large sum on an advertising campaign to launch a new product. While the benefit may last for a few years, this is generally treated as:
(A) An Intangible Asset
(B) A Fictitious Asset
(C) Revenue Expenditure
(D) Capital Expenditure

Ans :

(C) Revenue Expenditure

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Based on this, which of the following is NOT a capital receipt?
(A) ₹50,000 received as commission for services rendered.
(B) ₹5,000,000 raised by issuing new company shares.
(C) ₹200,000 received from selling an old office computer.
(D) ₹1,000,000 grant from the state government to build a warehouse.

Ans :

(A) ₹50,000 received as commission for services rendered.
The source text lists specific examples of capital receipts related to financing and investing activities. Commission received for services rendered is income from the day-to-day operations of the business. This is a revenue receipt, not a capital receipt, as it does not fit any of the categories mentioned in the source.

Oct/Nov 2013

91. A company acquired a patent for a new drug for ₹10,000,000. The journal entry to record this transaction, assuming payment by bank transfer, would involve:
(A) A debit to P&L Account and a credit to Bank Account.
(B) A debit to Bank Account and a credit to Asset (Patent Rights) Account.
(C) A debit to Asset (Patent Rights) Account and a credit to Bank Account.
(D) A debit to Purchases Account and a credit to Bank Account.

Ans :

(C) A debit to Asset (Patent Rights) Account and a credit to Bank Account.
A patent is an intangible asset. Its acquisition is a capital expenditure. The correct accounting entry is to debit the specific asset account (Patent Rights) to show an increase in assets and credit the Bank Account to show a decrease in cash. This follows the standard procedure for recording the acquisition of a fixed asset.

May/June 2015

92. Identify the incorrect pair from the following:
(A) Amount spent on routine repairs : Revenue Expenditure
(B) Profit on sale of machinery : Capital Receipt
(C) Amount received from sale of goods : Revenue Receipt
(D) Cost of installation of machinery : Capital Expenditure

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Ans :

(B) Profit on sale of machinery : Capital Receipt
The pair is incorrect because the profit on the sale of machinery is treated as a revenue-nature gain and is credited to the Profit & Loss Account. The total sale proceeds are the capital receipt, but the profit component itself is not. The other pairs correctly classify the respective items.

Oct/Nov 2012

93. If an expenditure helps to generate revenue over more than one accounting period, it is generally called:
(A) An Accrued Expense
(B) Operating Expense
(C) 'Capital Expenditure'
(D) Revenue Expenditure

Ans :

(C) 'Capital Expenditure'
This is a direct definitional test based on the 'Effect on Revenue Earning Capacity' criterion. An expenditure that provides benefits and helps generate revenue across multiple accounting periods is classified as a Capital Expenditure. The purchase of a plant is cited as a key example of this principle in action.

May/June 2011

94. Read the following excerpt: "Initial costs: These include purchase price including duties and non-refundable taxes, costs directly attributable to bringing the asset to the location and condition necessary for it to be operational."
A company imports a machine with a purchase price of ₹800,000. It pays ₹120,000 in non-refundable import duties and ₹30,000 for transportation. The capitalized cost of the machine is:
(A) ₹800,000
(B) ₹830,000
(C) ₹920,000
(D) ₹950,000

Ans :

(D) ₹950,000
Based on the provided text, the initial cost to be capitalized includes the purchase price (₹800,000), non-refundable taxes like import

May/June 2023

58. An amount spent on the replacement of a defective part of machinery is classified as:
(A) Revenue Expenditure
(B) Capital Expenditure
(C) Deferred Revenue Expenditure
(D) A charge against General Reserve

Ans :

(A) Revenue Expenditure
The replacement of a small, defective part of a machine is considered a repair and maintenance activity. This expenditure helps maintain the asset in its existing working condition but does not enhance its capacity or extend its useful life. Therefore, it is classified as a revenue expenditure and charged to the Profit & Loss account.

Oct/Nov 2018

59. Daily wages paid for the erection and installation of a new machinery should be treated as:
(A) Deferred Revenue Expenditure
(B) Prepaid Expense
(C) Capital Expenditure and debited to Machinery Account
(D) Revenue Expenditure and debited to Wages Account

Ans :

(C) Capital Expenditure and debited to Machinery Account
Any cost incurred to bring a new asset to its working condition for its intended use is capitalized. Wages paid specifically for the erection and installation of new machinery are directly attributable costs. Therefore, they are treated as capital expenditure and added to the cost of the machinery account, not expensed as wages.

May/June 2007

60. Which of the following statements is incorrect?
(A) Costs of relocating an entity's operations are capital expenditures.
(B) Underwriting commission for the issue of shares is a capital expenditure.
(C) Initial delivery and handling costs of an asset are capital expenditures.
(D) Costs of day-to-day servicing of an asset are revenue expenditures.

Ans :

(A) Costs of relocating an entity's operations are capital expenditures.
The statement that costs of relocating an entity's operations are capital expenditures is incorrect. Such costs are treated as revenue expenditures and are expensed in the period they are incurred. Underwriting commission is a cost of raising capital (capital expenditure), and initial delivery costs are capitalized as part of the asset's cost.

Oct/Nov 2025

61. For an expense to be classified as revenue or capital, it depends on:
(A) The kind of expense
(B) The duration of the benefit of the expenditure
(C) The effect on revenue earning capacity
(D) All of the above

Ans :

(D) All of the above
The classification of an expenditure is not based on a single criterion but a holistic view of several factors. These include the nature or kind of expense (recurring/non-recurring), the duration of its benefit (short-term/long-term), and its effect on the business's revenue-earning capacity (maintenance vs. enhancement). All these factors are considered together.

May/June 2012

62. Heavy expenditure on advertising a new product is an example of:
(A) Fictitious Asset
(B) Revenue Expenditure
(C) Intangible Asset
(D) Capital Expenditure

Ans :

(B) Revenue Expenditure
Although heavy advertising may provide benefits over a few years, accounting standards generally require such costs to be treated as revenue expenditure. This is because they fall under the category of costs for introducing a new product or service, which are expensed as incurred rather than being capitalized as an asset.

Oct/Nov 2014

63. Freight expenses of ₹25,000 paid for moving a newly purchased machinery to the factory is a:
(A) Revenue expense
(B) Deferred revenue expenditure
(C) Capital expenditure

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(D) Miscellaneous expense

Ans :

(C) Capital expenditure
Freight expenses incurred to transport a newly acquired asset to its place of installation are considered a directly attributable cost. These costs are necessary to bring the asset to the location and condition for its intended use. Therefore, they are capitalized, meaning they are added to the cost of the machinery asset itself.

May/June 2019

64. A company repaints its entire office building at a cost of ₹50,000. This expenditure does not increase the life or efficiency of the building. This cost should be:
(A) Debited to the Building Account
(B) Treated as a deferred revenue expenditure
(C) Capitalized and depreciated over 5 years
(D) Debited to the Repairs and Maintenance Account

Ans :

(D) Debited to the Repairs and Maintenance Account
Since the repainting does not enhance the building's earning capacity or extend its useful life, it is considered a maintenance expense. Its purpose is to maintain the asset's appearance and current condition. Therefore, it is a revenue expenditure and should be debited to the Repairs and Maintenance Account, an expense account in the P&L.

Oct/Nov 2006

65. Consider the following items:
1. Purchase of a new computer for office use
2. Annual software license renewal fee
3. Cost to upgrade the computer's RAM to improve performance
4. Monthly electricity bill for the office

Which of these are capital expenditures?
(A) 1 and 3 only
(B) 1, 2, and 3 only
(C) 1 only
(D) All of the above

Ans :

(A) 1 and 3 only
The purchase of a new computer (1) is the acquisition of a new asset. The RAM upgrade (3) enhances the performance and capacity of an existing asset. Both are capital expenditures. The annual license renewal (2) and the electricity bill (4) are recurring operational costs, making them revenue expenditures.

May/June 2021

66. Read the following excerpt: "A non-recurring expenditure is always capital in nature, unless materiality concept emphasises the importance of recognising it as revenue expenditure. Purchase of a wall clock for ₹500 is a non-recurring expenditure, but on the basis of the materiality concept, it may be treated as a revenue expense." Based on the excerpt, why might a ₹500 non-recurring purchase be treated as a revenue expense?
(A) Because wall clocks are not considered assets.
(B) Because the amount is considered insignificant.
(C) Because the payment was made in cash.
(D) Because it is a non-recurring expenditure.

Ans :

(B) Because the amount is considered insignificant.
The excerpt explicitly links the treatment of the ₹500 wall clock purchase as a revenue expense to the materiality concept. This concept allows for items of insignificant value to be expensed immediately for simplicity and convenience, even if they are technically capital in nature (non-recurring and providing long-term benefit).

Oct/Nov 2010

67. A manufacturing company spends ₹2,000,000 to purchase a new machine. It also pays ₹50,000 for transportation to the factory, ₹100,000 for installation, and ₹20,000 for testing the machine before it is put to use. What is the total amount that should be capitalized as the cost of the machine?
(A) ₹2,000,000
(B) ₹2,050,000
(C) ₹2,170,000
(D) ₹2,150,000

Ans :

(C) ₹2,170,000
The cost of a capital asset includes its purchase price plus all directly attributable costs to bring it to working condition. This includes transportation (₹50,000), installation (₹100,000), and testing costs (₹20,000). Therefore, the

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total capitalized cost is ₹2,000,000 + ₹50,000 + ₹100,000 + ₹20,000 = ₹2,170,000.

May/June 2005

68. Which of the following is an example of a capital loss?
(A) Loss incurred on the sale of a fixed asset
(B) Goods destroyed by fire
(C) Bad debts written off
(D) Discount allowed to customers

Ans :

(A) Loss incurred on the sale of a fixed asset
A loss on the sale of a fixed asset (where the selling price is less than the written down value) is considered a capital loss in nature, although it is charged to the Profit & Loss account. Goods destroyed by fire, bad debts, and discounts are all revenue losses arising from or related to normal business operations.

Oct/Nov 2022

69. Consider the following two statements regarding receipts:
Statement I : Receipts from day-to-day operations are called revenue receipts.
Statement II : Grants received from governments for building capital assets are revenue receipts.
(A) Both Statement I and Statement II are incorrect.
(B) Both Statement I and Statement II are correct.
(C) Only Statement I is correct.
(D) Only Statement II is correct.

Ans :

(C) Only Statement I is correct.
Statement I is correct as revenue receipts are generated from the main operating activities of a business. Statement II is incorrect because a grant received for the specific purpose of building a capital asset is non-recurring and is classified as a capital receipt, not a revenue receipt from operations.

May/June 2018

70. Which Ind AS deals with tangible assets such as property, and which deals with intangible assets, respectively?
(A) Ind AS 2 and Ind AS 16
(B) Ind AS 16 and Ind AS 38
(C) Ind AS 16 and Ind AS 2
(D) Ind AS 38 and Ind AS 16

Ans :

(B) Ind AS 16 and Ind AS 38
Indian Accounting Standard (Ind AS) 16, 'Property, Plant and Equipment', provides the accounting guidelines for tangible fixed assets. Indian Accounting Standard (Ind AS) 38, 'Intangible Assets', provides the guidelines for non-physical assets like software and patents. The question asks for the standards for tangible and intangible assets, respectively.

NODIA

Oct/Nov 2016

71. Read the following excerpt: "Costs which are not classified as Capital Expenditure":
"a. Costs of day-to-day servicing of the assets..."
"b. Costs of opening a new facility..."
"c. Costs of relocating or reorganizing part or all of an entity's operations."
Which of the following expenditures would be treated as a revenue expense based on this list?
(A) Cost of a major inspection of a plant.
(B) Purchase of a new delivery truck.
(C) Legal fees for the acquisition of a new office building.
(D) Marketing expenses for the launch of a new branch.

Ans :

(D) Marketing expenses for the launch of a new branch.
According to point 'b' in the source, costs of opening a new facility are not capitalized. Marketing expenses for a new branch launch fall under this category and are thus treated as revenue expenditure. The other options represent asset acquisition, directly attributable costs, and major subsequent costs, all of which are capitalized.

May/June 2014

72. A software company spends ₹500,000 on an extensive training program for its employees on a new programming language. This training is expected to improve the company's service delivery for the next two years. How should this ₹500,000 be treated?
(A) As a deferred revenue expenditure, written off over two years.
(B) As a revenue expenditure.
(C) As an intangible asset called 'Employee Skills'.
(D) As a capital expenditure, because the benefit lasts for two years.

Costs of introducing a new product, including advertising and promotional activities, are treated as revenue expenditure according to accounting standards. Even if the benefits may extend beyond one year, the uncertainty in quantifying future benefits leads to the conservative approach of expensing such costs as they are incurred. This falls under administrative and general costs.

May/June 2022

54. Match List-I with List-II and select the correct answer.

List-I (Type of Expenditure)

P. Cost of testing a new machine

Q. Cost of day-to-day servicing

R. Cost of relocating an office

S. Cost of replacing a major part of an asset

List-II (Classification)

1. Revenue Expenditure
2. Capital Expenditure

(A) P-2, Q-1, R-1, S-2

(B) P-1, Q-2, R-2, S-1

(C) P-2, Q-1, R-2, S-1

(D) P-1, Q-2, R-1, S-2

Ans :

(A) P-2, Q-1, R-1, S-2

P (Testing cost) and S (Major part replacement) are capitalized as they are necessary to make the asset operational or enhance it. They are Capital Expenditures (2). Q (Day-to-day servicing) and R (Relocation costs) are operational expenses and do not create a long-term asset. They are Revenue Expenditures (1).

Oct/Nov 2023

55. Which of the following would be classified as a capital receipt for a business?

(A) A long-term loan received from a financial institution

(B) Cash received from a debtor

(C) Commission received

(D) Sale of scrap material

Ans :

(A) A long-term loan received from a financial institution

A long-term loan received from a financial institution is a capital receipt because it is not generated from the company's ordinary operating activities and it creates a long-term liability on the balance sheet. Cash from debtors, commission, and sale of scrap are all examples of revenue receipts arising from normal business operations.

May/June 2016

56. Consider the following statements:

1. Expenditure on research is always a capital expenditure.
2. Expenditure on staff training to operate an asset is a revenue expenditure.
3. Costs of opening a new facility are treated as capital expenditure.

Which of the above statements is/are correct?

(A) 2 and 3 only

(B) 2 only

(C) 1, 2 and 3

(D) 1 and 3 only

Ans :

(B) 2 only

Statement 2 is correct as staff training costs are expensed as revenue expenditure. Statement 1 is incorrect because research costs are generally treated as revenue expenditure. Statement 3 is incorrect because costs of opening a new facility or conducting business in a new location are classified as revenue expenditure, not capital.

Oct/Nov 2009

57. Consider the following statements:

Assertion (A): Amount received from the sale of goods is a revenue receipt.

Reason (R) : This receipt arises from the day-to-day operations of the company.

(A) Both A and R are true, and R is the correct explanation of A.

(B) Both A and R are true, but R is not the correct explanation of A.

(C) A is true, but R is false.

(D) A is false, but R is true.

Ans :

(A) Both A and R are true, and R is the correct explanation of A.

The assertion that the sale of goods results in a revenue receipt is correct. The reason given is that this receipt stems from the principal, day-to-day operating activities of the business. This is the precise definition of a revenue receipt, making the reason a correct explanation for the assertion.

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treated as a revenue expenditure and charged to the P&L account.

Oct/Nov 2011

77. A firm purchases a building for ₹10,000,000. It pays an additional ₹500,000 as brokerage fees and ₹700,000 in non-refundable registration taxes. Immediately after purchase, it spends ₹200,000 on painting the office interiors. What is the total capital expenditure to be recorded for the building?

(A) ₹10,000,000
(B) ₹10,500,000
(C) ₹11,200,000
(D) ₹11,400,000

Ans :

(C) ₹11,200,000
The capital cost includes the purchase price (₹10,000,000) plus all directly attributable costs like brokerage (₹500,000) and non-refundable taxes (₹700,000). The painting cost (₹200,000) is a routine maintenance expense and is treated as revenue expenditure. Thus, the total capital expenditure is ₹10,000,000 + ₹500,000 + ₹700,000 = ₹11,200,000.

May/June 2010

78. Which of the following statements about receipts is correct?

(A) Revenue receipts are routed through the Profit & Loss Account.
(B) All receipts are treated as income.
(C) Capital receipts are recurring in nature.
(D) Sale of a fixed asset at its book value results in a revenue receipt.

Ans :

(A) Revenue receipts are routed through the Profit & Loss Account.
Revenue receipts, which arise from the day-to-day operations of a business, are used to calculate the profit or loss for a period and are therefore routed through the Profit & Loss Account. The other statements are incorrect. Not all receipts are income (e.g., loans); capital receipts are non-recurring; and sale proceeds are capital receipts.

Oct/Nov 2024

79. Match List-I (Transaction) with List-II (Classification).
List-I
P. Sale of goods
Q. Sale of old car
R. Interest received on bank deposit
S. Loan from bank
List-II
1. Capital Receipt
2. Revenue Receipt
(A) P-2, Q-1, R-2, S-1
(B) P-1, Q-2, R-1, S-2
(C) P-2, Q-1, R-1, S-2
(D) P-1, Q-2, R-2, S-1

NODIA

Ans :

(A) P-2, Q-1, R-2, S-1
Sale of goods (P) and Interest received (R) are from normal operations, hence they are Revenue Receipts (2). Sale of an old car (Q), a fixed asset, and a loan from a bank (S) are non-operational, long-term financing or investing activities, hence they are Capital Receipts (1).

May/June 2017

80. An expenditure that does not result in the acquisition of a permanent asset but whose benefits are spread over several years is known as:

(A) An item treated as revenue expenditure, as a separate category is not defined in the provided material
(B) Capital Expenditure, as the long-term benefit requires it to be capitalized as an asset
(C) A contingent asset, as the future economic benefits are uncertain and not fully controlled
(D) Deferred Revenue Expenditure, a specific classification for large, non-asset-forming expenses

Ans :

(A) An item treated as revenue expenditure, as a separate category is not defined in the provided material
The provided text does not use or define the term "Deferred Revenue Expenditure." It classifies costs like opening a new facility or advertising, whose benefits might last longer than a year, as revenue expenditures to be expensed as incurred. Therefore, based strictly on the provided material, such items are treated as revenue expenditures.

Oct/Nov 2005

81. According to the table "DISTINCTION BETWEEN CAPITAL AND REVENUE EXPENDITURE", which of the following is a stated characteristic of Revenue Expenditure?

(A) The benefit is of long duration.
(B) It is recurring.
(C) The purpose is to improve or enhance business capacity.
(D) The amount spent is usually large.

Ans :

(B) It is recurring.
The table explicitly lists five points of distinction. For revenue expenditure, point (4) states that it is "recurring". The other options listed (large amount, long duration benefit, enhancing capacity) are all characteristics attributed to capital expenditure in the same table, making them incorrect descriptions of revenue expenditure according to the source.

May/June 2020

82. A company, ABC Ltd, has a machine with a book value of ₹80,000. It sells the machine for ₹100,000. How would the ₹100,000 receipt and the ₹20,000 profit be classified?
(A) ₹100,000 is a capital receipt; ₹20,000 is a revenue nature profit recorded in P&L.
(B) ₹100,000 is a revenue receipt; ₹20,000 is a capital profit.
(C) Both are capital receipts.
(D) Both are revenue receipts.

Ans :

(A) ₹100,000 is a capital receipt; ₹20,000 is a revenue nature profit recorded in P&L.
The total proceeds from the sale of a fixed asset (₹100,000) are a capital receipt. However, the profit or loss on such a sale is considered a revenue item. The profit of ₹20,000 (₹100,000 - ₹80,000) must be recognized in the Profit & Loss account for the period.

Oct/Nov 2015

83. Which of the following costs is explicitly mentioned as being treated as revenue expenditure?
(A) Costs of testing an asset.
(B) Professional fees for asset acquisition.
(C) Selling, administrative and other general overheads.
(D) Research of development expenditure.

Ans :

(C) Selling, administrative and other general overheads.
The text, under section 7.2.3(d), lists costs not classified as capital expenditure. It specifies that costs on internally generated assets, including "selling, administrative and other general overheads," are treated as revenue expenditure. The other options are listed as examples of costs that are classified as capital expenditure under section 7.2.2.

May/June 2013

84. The primary objective of distinguishing between capital and revenue items is to:
(A) Simplify the overall bookkeeping process and reduce clerical work
(B) Comply with the specific format requirements of the company's auditors
(C) Legally minimize the income tax liability of the business for the period
(D) Ascertain correct profit and present a true and fair view of financial position

Ans :

(D) Ascertain correct profit and present a true and fair view of financial position
The introduction section emphasizes this distinction's importance in preparing final accounts. Correctly classifying items ensures that only revenue items are matched in the P&L account to find the period's profit, and capital items are correctly placed in the balance sheet, thus presenting a true and fair view of performance and position.

Oct/Nov 2021

85. As per section 7.2.2, subsequent costs are classified as capital expenditure. This includes "costs of parts of some items of the assets requiring replacement at regular intervals" and "costs of major inspections for potential faults". Which of the following would be capitalized based on this?
(A) The cost of replacing the engine of a truck every five years.
(B) The cost of oiling a machine weekly.
(C) The cost of cleaning the factory premises daily.
(D) The cost of replacing a fused lightbulb in the office.

Ans :

(A) The cost of replacing the engine of a truck every five years.

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The source identifies the replacement of major parts at regular intervals as a capital expenditure. Replacing a truck's engine every five years fits this description perfectly, as it's a significant component replacement. The other options represent minor, day-to-day servicing or repairs, which are treated as revenue expenditures.

May/June 2024

86. A bookstore chain, "Readers' Haven," reorganizes its operations by closing two small stores and opening one large superstore. The costs associated with closing the old stores and moving inventory amount to ₹300,000. How should this expenditure be treated?

(A) As an intangible asset for business reorganization.
(B) As revenue expenditure.
(C) As a loss on disposal of the old stores.
(D) As capital expenditure, since it relates to a new superstore.

Ans :

(B) As revenue expenditure.
According to section 7.2.3(c), "Costs of relocating or reorganizing part or all of an entity's operations" are not classified as capital expenditure. These are treated as revenue expenditures and are expensed in the period they are incurred, even if they are part of a larger strategic shift like opening a new superstore.

Oct/Nov 2008

87. An expenditure on the acquisition of an intangible asset like computer software is treated as:

(A) A deferred revenue expenditure.
(B) A miscellaneous expenditure.
(C) A capital expenditure.
(D) A revenue expenditure because it is intangible.

Ans :

(C) A capital expenditure.
The text clearly states that capital expenditure relates not only to tangible fixed assets but also to intangible assets like computer software and patent rights. Since software provides benefits over many years, its acquisition cost is capitalized and shown as an asset on the balance sheet, governed by Ind AS 38.

May/June 2006

88. Consider the following four statements:

1. Capital expenditure is shown in the profit and loss account.
2. Revenue expenditure is non-recurring.
3. The benefit from capital expenditure is of long duration.
4. The amount spent on revenue expenditure is usually large.

How many of the above statements are correct?

(A) One
(B) Two
(C) Three
(D) Four

Ans :

(A) One
Only statement 3 is correct. Capital expenditure benefits last for a long duration. Statement 1 is incorrect (it's in the Balance Sheet). Statement 2 is incorrect (revenue expenditure is recurring). Statement 4 is incorrect (revenue expenditure amount is relatively small compared to capital). Therefore, only one statement is correct.

Oct/Nov 2017

89. Which of the following is the most appropriate description of a revenue expenditure?

(A) A large, one-time payment for a non-physical asset.
(B) An expenditure incurred to acquire assets for resale.
(C) An expenditure whose benefit is consumed within the current accounting period.
(D) An expenditure that increases the earning capacity of the business.

Ans :

(C) An expenditure whose benefit is consumed within the current accounting period.
The most accurate and fundamental description of a revenue expenditure is that its benefits are exhausted within the current accounting period. This is why it is matched against the revenues of the same period in the Profit & Loss Account. Other descriptions may be partially true in some contexts but are not as universally applicable.

May/June 2008

90. Read the following excerpt: "Capital Receipts are from issue of Equity/Preference shares/Capital Instruments or from sale or Disposal of Fixed Assets/Long Term investments or from Grants received from Governments for building of Capital Assets."

NODIA

Ans :

(B) As a revenue expenditure.
Despite the potential for long-term benefits, expenditure on training staff is explicitly classified as a revenue expenditure. Accounting standards do not permit the capitalization of such costs, as they are not directly related to creating or producing a specific recognizable asset. They are considered operational costs and are expensed as incurred.

Oct/Nov 2007

73. Identify the correct combination of statements regarding capital expenditure.
1. It is shown in the balance sheet.
2. The benefit is of short duration.
3. The purpose is to maintain assets in good working condition.
4. The amount spent is usually large.

(A) 2 and 3 are correct.
(B) 3 and 4 are correct.
(C) 1 and 4 are correct.
(D) 1 and 2 are correct.

Ans :

(C) 1 and 4 are correct.
Correct characteristics of capital expenditure are that it is shown in the balance sheet (as an asset) and the amount involved is usually large. The benefit is of long duration (not short), and its purpose is to enhance capacity, not just maintain assets (which is the purpose of revenue expenditure).

May/June 2025

74. Which of the following is NOT a source of capital receipts?
(A) Grants received from Governments for building Capital Assets
(B) Sale of Long-Term investments
(C) Issue of Preference shares
(D) Interest received on investments

Ans :

(D) Interest received on investments
Interest received on investments is income earned from holding a financial asset as part of the company's regular activities. It is a recurring income and is therefore classified as a revenue receipt, to be credited to the Profit & Loss account. The other options are all non-recurring transactions that affect the capital structure or long-term assets.

Oct/Nov 2019

75. Consider the following statements:
Assertion (A): The cost of replacing a small, worn-out part of a machine is a revenue expense.
Reason (R) : The expenditure is incurred to maintain the earning capacity of the asset, not to enhance it.
(A) Both A and R are true, and R is the correct explanation of A.
(B) Both A and R are true, but R is not the correct explanation of A.
(C) A is true, but R is false.
(D) A is false, but R is true.

Ans :

(A) Both A and R are true, and R is the correct explanation of A.
The assertion is correct; replacing a small part is a repair, which is a revenue expense. The reason correctly explains why: the expense is for maintenance (maintaining earning capacity) rather than for an upgrade (enhancing earning capacity). This distinction is the core principle for classifying repairs as revenue expenditure.

May/June 2009

76. Read the following excerpt: "Costs on internally generated assets like Goodwill, Brands, Mastheads, Publishing titles, Customer lists and similar items, if the costs are not directly related to create, produce and operate these. Such costs include: selling, administrative and other general overheads..."
Based on this, how should a company treat the ₹1,000,000 it spent on a nationwide brand-building advertising campaign?
(A) Defer it over the expected life of the brand.
(B) Treat it as a revenue expenditure.
(C) Show it as a reduction from share capital.
(D) Capitalize it as an intangible asset 'Brand'.

Ans :

(B) Treat it as a revenue expenditure.
The text explicitly states that costs on internally generated brands, including selling and administrative overheads (like advertising), are not capitalized. Such expenditures are difficult to measure reliably and are expensed as incurred. Therefore, the brand-building campaign cost is

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duties (₹120,000), and directly attributable costs like transportation (₹30,000). The total capitalized cost is the sum of these amounts: ₹800,000 + ₹120,000 + ₹30,000 = ₹950,000.

Oct/Nov 2020

95. A firm owns a fleet of delivery vans. It spends ₹10,000 on a major overhaul of one van's engine, which is expected to increase its fuel efficiency and extend its life by two years. It also spends ₹500 on replacing a broken taillight on another van. How are these expenditures classified?

(A) ₹10,000 is capital expenditure; ₹500 is revenue expenditure.
(B) Both are capital expenditures.
(C) Both are revenue expenditures.
(D) ₹10,000 is revenue expenditure; ₹500 is capital expenditure.

Ans :

(A) ₹10,000 is capital expenditure; ₹500 is revenue expenditure.
The major overhaul (₹10,000) enhances the asset's performance and extends its life, making it a capital expenditure. The replacement of a broken taillight (₹500) is a minor repair to restore the van to its normal working condition, making it a revenue expenditure. This illustrates the difference between enhancement and maintenance.

May/June 2022

96. Which of the following statements correctly differentiates between capital and revenue receipts?

(A) Capital receipts reduce liabilities, while revenue receipts increase assets.
(B) Capital receipts are not routed through the P&L account, while revenue receipts are.
(C) Capital receipts arise from day-to-day operations, while revenue receipts do not.
(D) Capital receipts are recurring, while revenue receipts are non-recurring.

Ans :

(B) Capital receipts are not routed through the P&L account, while revenue receipts are.
The primary accounting difference is their treatment in the final accounts. Revenue receipts are part of the income statement (P&L Account) to calculate profit. Capital receipts, like share issuance or asset sales, are non-operational and directly impact the balance sheet without passing through the P&L account (except for any profit/loss element).

Oct/Nov 2023

97. Which of the following expenditures would be debited to the Profit and Loss Account?

(A) Cost of installing air conditioners in a new office.
(B) Legal expenses incurred on the purchase of land.
(C) Monthly salaries paid to office staff.
(D) Purchase of a new building.

Ans :

(C) Monthly salaries paid to office staff.
Monthly salaries are a recurring operational cost incurred to run the business. This is a classic revenue expenditure and is therefore debited to the Profit and Loss Account. The other options are all capital expenditures related to the acquisition and preparation of fixed assets, which would be debited to asset accounts.

May/June 2016

98. Read the following excerpt: The text states that costs of "conducting business in a new location or with a new class of customers" are treated as revenue expenditure. A bank traditionally serving retail customers spends ₹2,000,000 on market research and creating new processes to start serving high-net-worth corporate clients. This expenditure should be:

(A) Treated as revenue expenditure.
(B) Capitalized as an intangible asset.
(C) Deferred over 5 years.
(D) Set off against the profits from the new customer class.

Ans :

(A) Treated as revenue expenditure.
The source text explicitly categorizes costs associated with conducting business with a new class of customers as revenue expenditure. Therefore, the ₹2,000,000 spent to enter the corporate client market should be expensed in the period it is incurred, not capitalized or deferred, regardless of the expected future benefits.

NODIA

Oct/Nov 2009

99. A company issues 100,000 equity shares of ₹10 each at a premium of ₹2 per share. It also sells old furniture for ₹50,000 (book value ₹40,000). What

(C) P-2, Q-1, R-3, S-4
(D) P-4, Q-3, R-1, S-2

Ans :

(A) P-2, Q-3, R-1, S-4
Purchase of Building (P) is a capital expenditure, shown on the Asset side of the Balance Sheet (2). Salary Paid (Q) is a revenue expense, shown on the Debit side of the P&L Account (3). Sales Revenue (R) is a revenue receipt, shown on the Credit side of the P&L Account (1). Share Capital (S) is a capital receipt, shown on the Liability side of the Balance Sheet (4).

Oct/Nov 2010

109. Which of the following is considered a revenue expenditure?
(A) Initial delivery and handling costs for a new asset.
(B) Research of development expenditure.
(C) Costs of labour and consumables for day-to-day servicing of assets.
(D) Costs of testing a newly acquired machine.

Ans :

(C) Costs of labour and consumables for day-to-day servicing of assets.
As per section 7.2.3(a), the costs of day-to-day servicing of assets, which include labour and consumables, are explicitly classified as revenue expenditure. The other options—testing costs, certain development expenditure, and initial delivery costs—are all listed as examples of costs that are classified as capital expenditure under section 7.2.2.

May/June 2005

110. The accounting entry for the acquisition of an intangible asset like a patent for cash would be:
(A) Debit Patent A/c, Credit Cash A/c
(B) Debit Purchases A/c, Credit Cash A/c
(C) Debit P&L A/c, Credit Cash A/c
(D) Debit Cash A/c, Credit Patent A/c

Ans :

(A) Debit Patent A/c, Credit Cash A/c
The purchase of a patent is a capital expenditure. The correct accounting treatment is to recognize the intangible asset by debiting the Patent account. Since cash is paid, the Cash account is credited to reflect the outflow of funds. This correctly records the increase in intangible assets and the decrease in cash.

Oct/Nov 2022

111. Read the following excerpt: The introduction states, "All expenses and receipts of revenue nature are shown in the trading and profit and loss account and all expenses and receipts of a capital nature are taken to the balance sheet."
Based on this rule, where would the proceeds from a long-term bank loan be recorded?
(A) In the trading account as a receipt.
(B) In the profit and loss account as an expense.
(C) In the profit and loss account as income.
(D) In the balance sheet as a liability.

Ans :

(D) In the balance sheet as a liability.
A long-term bank loan is a financing activity, not an operational one. It is a capital receipt that creates a liability for the company. According to the rule stated in the source, receipts of a capital nature are taken to the balance sheet. Therefore, the loan would be recorded as a liability.

May/June 2018

112. A company spends ₹2,000,000 on research to discover a new chemical compound. It then spends an additional ₹5,000,000 on development activities that meet the criteria for capitalization under Ind AS 38. How are these expenditures classified?
(A) Both are revenue expenditures.
(B) ₹2,000,000 is revenue expenditure; ₹5,000,000 is capital expenditure.
(C) ₹2,000,000 is capital expenditure; ₹5,000,000 is revenue expenditure.
(D) Both are capital expenditures.

Ans :

(B) ₹2,000,000 is revenue expenditure; ₹5,000,000 is capital expenditure.
While the text lists "Research of development expenditure" as an example of capital cost, accounting standards (like Ind AS 38) typically require research costs to be expensed as incurred (revenue expenditure). Certain development costs can be capitalized if specific criteria are met. Thus, the research is revenue, and the qualifying development is capital.

Oct/Nov 2016

113. The main purpose of incurring revenue expenditure is to:
(A) Acquire a fixed asset for long-term use.
(B) Increase the earning capacity of the business

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be treated as a revenue expense.

(A) Both Statement I and Statement II are incorrect.
(B) Both Statement I and Statement II are correct.
(C) Only Statement I is correct.
(D) Only Statement II is correct.

Ans :

(D) Only Statement II is correct.
Statement II is correct, as exemplified by the purchase of a ₹500 wall clock. Statement I is incorrect because it misses the exception provided by the materiality concept. A non-recurring expenditure is usually capital, but not always without exception, as small, immaterial amounts can be expensed for practical reasons.

Oct/Nov 2014

105. A business receives a ₹50,000 insurance claim for inventory destroyed in a fire. How should this receipt be treated?

(A) As a reduction from the insurance expense account.
(B) As a direct credit to the capital account.
(C) As a revenue receipt, as it compensates for the loss of a current asset (inventory).
(D) As a capital receipt, since it is non-recurring.

Ans :

(C) As a revenue receipt, as it compensates for the loss of a current asset (inventory).
The insurance claim is received to compensate for the loss of inventory, which is a current asset and part of the business's normal operating cycle. The loss of stock is a revenue loss, and therefore the compensation received against it is treated as a revenue receipt, which is credited to the Profit & Loss Account.

May/June 2019

106. Which of the following costs associated with an internally generated intangible asset would be capitalized?

(A) Costs of advertising to promote the asset.
(B) All directly attributable costs necessary to create, produce, and operate the asset.
(C) Selling and administrative overheads incurred during its development.
(D) Expenditure on training staff to operate the asset.

Ans :

(B) All directly attributable costs necessary to create, produce, and operate the asset.
While costs like staff training, selling overheads, and advertising for internally generated assets are expensed as revenue expenditure, the text specifies an exception. "All directly attributable costs necessary to create, produce and operate an internally generated intangible asset" are classified as capital expenditure. This is a key distinction made under Ind AS 38.

Oct/Nov 2006

107. Consider the following statements:
Assertion (A): The cost of reorganizing a company's sales department is treated as a revenue expenditure.
Reason (R) : This cost does not create a new asset or enhance the value of an existing one.

(A) Both A and R are true, and R is the correct explanation of A.
(B) Both A and R are true, but R is not the correct explanation of A.
(C) A is true, but R is false.
(D) A is false, but R is true.

Ans :

(A) Both A and R are true, and R is the correct explanation of A.
The assertion that reorganization costs are revenue expenditure is correct, as stated in section 7.2.3(c). The reason provided is also correct; such costs are expensed because they do not meet the criteria for capitalization, which require the creation or enhancement of a recognizable asset. The reason correctly explains the accounting treatment.

May/June 2021

108. Match List-I (Item) with List-II (Classification in Final Accounts).

List-I
P. Purchase of Building
Q. Salary Paid
R. Sales Revenue
S. Share Capital Issued

List-II
1. Credit side of P&L Account
2. Asset side of Balance Sheet
3. Debit side of P&L Account
4. Liability side of Balance Sheet

(A) P-2, Q-3, R-1, S-4
(B) P-4, Q-1, R-3, S-2

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(A) Capital Receipt
(B) Revenue Receipt
(C) Other Income
(D) Extraordinary Item

Ans :

(A) Capital Receipt
A loan, regardless of the source, is a financing activity that increases the company's liabilities. It is not income from day-to-day operations. Therefore, it is classified as a capital receipt and will be shown as a liability on the balance sheet, not as income in the profit and loss account.

Oct/Nov 2008

129. The distinction between capital and revenue is necessary for the preparation of which final accounts?
(A) The Cash Flow Statement only.
(B) The Bank Reconciliation Statement.
(C) The Trading and Profit and Loss Account and the Balance Sheet.
(D) The Trial Balance only.

Ans :

(C) The Trading and Profit and Loss Account and the Balance Sheet.
The introduction highlights that this distinction is crucial for preparing the final accounts. Revenue items go to the Trading and P&L Account to determine profit, while capital items go to the Balance Sheet to reflect the financial position. Correct classification is fundamental to both these key financial statements.

May/June 2006

130. A company spends ₹20,000 on customs duty and ₹10,000 on freight for importing a new machine. How should these amounts be treated?
(A) Both as capital expenditures, added to the cost of the machine.
(B) Both as revenue expenditures.
(C) Customs duty as capital and freight as revenue.
(D) Freight as capital and customs duty as revenue.

Ans :

(A) Both as capital expenditures, added to the cost of the machine.
Both customs duty (a non-refundable tax) and freight (an initial delivery cost) are directly attributable costs incurred to bring the asset to its working condition. According to the principles outlined, such costs are not expensed immediately but are capitalized, meaning they are added to the initial cost of the machine on the balance sheet.

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permanently.
(C) Support the day-to-day operational activities of the business.
(D) Pay off long-term debts and liabilities.

Ans :

(C) Support the day-to-day operational activities of the business.
Revenue expenditures are costs related to the core operations of a business within an accounting period. Their purpose is to maintain the business as a going concern, generate the current period's revenue, and maintain existing assets, rather than acquiring new ones or fundamentally enhancing capacity for the long term.

May/June 2014

114. The purchase of office stationery for ₹5,000 is an example of:
(A) Capital Loss
(B) Deferred Revenue Expenditure
(C) Capital Expenditure
(D) Revenue Expenditure

Ans :

(D) Revenue Expenditure
Office stationery is a consumable item used in the day-to-day running of the business. The benefit from this expenditure is consumed within a short period, typically the current accounting year. It is a recurring operational cost and is therefore a classic example of a revenue expenditure.

Oct/Nov 2007

115. Identify the correct statement regarding Ind AS 16 and Ind AS 38.
(A) Ind AS 16 covers property, plant, and equipment, while Ind AS 38 covers intangible assets.
(B) Ind AS 16 deals with intangible assets, while Ind AS 38 deals with tangible assets.
(C) Both standards deal with revenue expenditure only.
(D) Both standards mandate that all related costs must be treated as revenue expenses.

Ans :

(A) Ind AS 16 covers property, plant, and equipment, while Ind AS 38 covers intangible assets.
The text explicitly mentions that Ind AS 16 deals with tangible fixed assets like property, plant, and equipment, and Ind AS 38 deals with intangible assets. These standards provide the framework for classifying costs associated with these assets as either capital or revenue, guiding their accounting treatment.

May/June 2025

116. Read the following excerpt: The text lists "Professional fees" as an example of costs classified as capital expenditure. In which context are such fees considered capital?
(A) When paid for annual tax filing.
(B) When paid to an engineer for supervising the construction of a new asset.
(C) When paid for routine legal advice.
(D) When paid to a consultant for a monthly operational review.

Ans :

(B) When paid to an engineer for supervising the construction of a new asset.
The context for capitalizing professional fees is their direct relationship with the acquisition or construction of a capital asset. Fees paid to an engineer for supervising construction are a directly attributable cost of that asset. Fees for routine advice, tax filing, or operational reviews are revenue expenses as they relate to ongoing operations.

Oct/Nov 2019

117. A company's trial balance shows a debit balance for 'Plant and Machinery' and a credit balance for 'Sales'. At the year-end, where will these balances be carried forward to?
(A) 'Plant and Machinery' to the Balance Sheet and 'Sales' to the Trading and Profit and Loss Account.
(B) Both to the Balance Sheet.
(C) Both to the Trading and Profit and Loss Account.
(D) 'Plant and Machinery' to the Trading and Profit and Loss Account and 'Sales' to the Balance Sheet.

Ans :

(A) 'Plant and Machinery' to the Balance Sheet and 'Sales' to the Trading and Profit and Loss Account.
'Plant and Machinery' represents a capital expenditure (asset) and is therefore taken to the asset side of the Balance Sheet. 'Sales' is a revenue receipt (income) and is taken to the credit side of the Trading and Profit and Loss Account. This

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follows the fundamental principle of preparing final accounts.

May/June 2009

118. Which of the following is an example of a recurring expenditure?
(A) Payment of monthly rent
(B) Purchase of a new building
(C) Purchase of a long-term investment
(D) Cost of installing a new production line

Ans :

(A) Payment of monthly rent
A recurring expenditure is one that occurs frequently in the normal course of business. Payment of monthly rent is a regular, operational cost. The other options—purchase of a building, investment, or production line—are all examples of non-recurring transactions that are typically classified as capital expenditures.

Oct/Nov 2011

119. An amount received from a 'Capital Instrument' is classified as a:
(A) Contra Receipt
(B) Deferred Revenue Receipt
(C) Capital Receipt
(D) Revenue Receipt

Ans :

(C) Capital Receipt
The text under section 7.4.1 explicitly states that Capital Receipts are from the issue of "Equity/Preference shares/Capital Instruments". Therefore, any proceeds from issuing such instruments are, by definition, considered capital receipts as they relate to the financing and capital structure of the company rather than its daily operations.

May/June 2010

120. Which statement is true regarding the accounting of capital expenditure?
(A) It is recorded as an asset on the Balance Sheet.
(B) It is immediately charged as an expense in the Profit & Loss account.
(C) It is ignored in the books of accounts until the asset is sold.
(D) It is credited to the asset account.

Ans :

(A) It is recorded as an asset on the Balance Sheet.
When a capital expenditure is incurred, it results in the acquisition of an asset that will provide future economic benefits. Therefore, it is not expensed immediately. Instead, it is recorded as an asset on the balance sheet and its cost is typically spread over its useful life through depreciation.

Oct/Nov 2024

121. Which one of the following is incorrect as per the distinction table?
(A) The benefit of capital expenditure is of long duration.
(B) Capital expenditure is shown in the balance sheet.
(C) Revenue expenditure is recurring.
(D) The amount spent on revenue expenditure is usually large.

Ans :

(D) The amount spent on revenue expenditure is usually large.
According to the distinction table provided, the amount spent on revenue expenditure is "relatively small," whereas the amount spent on capital expenditure is "usually large." Therefore, the statement that the amount spent on revenue expenditure is usually large is incorrect based on the provided text.

May/June 2017

122. Costs of employee benefits arising directly from the construction or acquisition of an asset are an example of:
(A) Prepaid expense
(B) Capital expenditure
(C) Accrued liability
(D) Revenue expenditure

Ans :

(B) Capital expenditure
The text explicitly lists "Costs of employee benefits arising directly from the construction or acquisition of the asset" as an example of costs that are classified as capital expenditure. This means wages and salaries of workers directly involved in creating the asset are added to the cost of that asset.

Oct/Nov 2005

123. Which of the following correctly describes the 'effect on revenue earning capacity' test?
(A) If it has a direct effect on revenue, it's

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revenue; if indirect, it's capital.
(B) If it has no effect on revenue, it's capital.
(C) If it affects the current year's revenue, it's revenue; if it affects future years' revenue, it's capital.
(D) If it increases revenue, it's capital; if it decreases revenue, it's revenue expenditure.

Ans :

(C) If it affects the current year's revenue, it's revenue; if it affects future years' revenue, it's capital.
This test focuses on the timing of the revenue generation linked to the expense. Expenses that help generate revenue in the current period are matched against that revenue and are thus classified as revenue expenditure. Expenses that help generate revenue over multiple future periods are capitalized as assets.

May/June 2020

124. Read the following excerpt: The text states that costs of "introducing a new product or service" are treated as revenue expenditure. A tech company spends ₹1,000,000 on a launch event and initial marketing for its new mobile application. This cost should be:
(A) Recorded as an intangible asset called 'Marketing Rights'.
(B) Deferred and written off over three years.
(C) Capitalized as part of the software's cost.
(D) Treated as revenue expenditure and expensed immediately.

Ans :

(D) Treated as revenue expenditure and expensed immediately.
The source text is clear that costs related to introducing a new product or service are not capitalized but are treated as revenue expenditure. The launch event and marketing costs fall directly into this category. Therefore, the ₹1,000,000 must be charged to the Profit & Loss account in the period it is incurred.

Oct/Nov 2015

125. A transport company purchases a new truck for ₹2,500,000. The entry in its books would be a debit to the 'Truck Account' and a credit to the 'Bank/Creditor Account'. The 'Truck Account' will appear in which financial statement?
(A) On the asset side of the Balance Sheet.
(B) On the debit side of the Profit & Loss Account.
(C) On the credit side of the Trading Account.
(D) On the liability side of the Balance Sheet.

Ans :

(A) On the asset side of the Balance Sheet.
The purchase of a truck is a capital expenditure, creating a fixed asset. The 'Truck Account' represents this asset. Assets are shown on the asset side of the Balance Sheet, which reflects the financial position of the company at a specific point in time. It is not an expense to be shown in the P&L.

May/June 2013

126. Which of the following is NOT a characteristic of revenue expenditure?
(A) Amount spent is relatively small.
(B) It is shown in the balance sheet.
(C) It is recurring.
(D) Benefit is of short duration.

Ans :

(B) It is shown in the balance sheet.
Revenue expenditure is shown in the Profit and Loss Account, not the balance sheet. It is an expense matched against the revenue of the current period. The other three options—short-duration benefit, recurring nature, and relatively small amount—are all correctly listed as characteristics of revenue expenditure in the distinction table.

Oct/Nov 2021

127. Which of the following is a capital expenditure?
(A) Wages paid to factory workers.
(B) Office electricity bill.
(C) Purchase of a trademark.
(D) Annual insurance on machinery.

Ans :

(C) Purchase of a trademark.
A trademark is an intangible asset that provides exclusive rights and benefits to the business over a long period. Its purchase is a non-recurring event that enhances the company's market position. Therefore, it is a capital expenditure. Wages, electricity, and insurance are all recurring operational costs classified as revenue expenditures.

May/June 2024

128. If a company receives ₹500,000 as a loan from its director, this receipt is classified as:

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credit between buyers and sellers or lenders and borrowers.

Oct/Nov 2010

5. According to Section 5 of the Negotiable Instruments Act, which of the following is an essential characteristic of a Bill of Exchange?
(A) It must contain a conditional order.
(B) It can be an oral agreement.
(C) It must be an order to pay a certain sum of money only.
(D) It is signed by the payee.

Ans :

(C) It must be an order to pay a certain sum of money only.
A Bill of Exchange is defined as an instrument in writing containing an unconditional order, signed by the maker, to pay a certain sum of money only. The payment cannot be linked to goods or other forms of consideration; it must be exclusively a monetary payment. This ensures the instrument's negotiability and clear value.

May/June 2025

6. In the context of a bill of exchange, who is the 'Drawee'?
(A) The person who is going to receive the money.
(B) The person on whom the bill is drawn.
(C) The person who draws the bill.
(D) The person who endorses the bill to another party.

Ans :

(B) The person on whom the bill is drawn.
A bill of exchange involves three parties. The 'Drawer' is the person who creates or draws the bill. The 'Drawee' is the party on whom the bill is drawn and who is ordered to make the payment. The 'Payee' is the person who is entitled to receive the payment. The drawee becomes the acceptor upon signing the bill.

Oct/Nov 2016

7. Under what circumstance can the drawer and the payee of a bill of exchange be the same person?
(A) When the bill is discounted with a bank.
(B) When the bill is drawn for accommodation purposes.
(C) This is not possible under the Negotiable Instruments Act.
(D) When the drawer intends to receive the payment themselves.

Ans :

(D) When the drawer intends to receive the payment themselves.
The drawer is the maker of the bill, and the payee is the recipient of the money. If the drawer creates a bill and makes it payable to themselves or their order, they function as both the drawer and the payee. This is a common scenario, especially in trade transactions where a seller draws a bill on a buyer.

May/June 2011

8. In a typical trade transaction, what is the relationship between the person who draws a bill of exchange and the person on whom it is drawn?
(A) The drawer is the creditor, and the drawee is the debtor.
(B) The drawer is the debtor, and the drawee is the creditor.
(C) Both parties are creditors.
(D) There is no debtor-creditor relationship.

Ans :

(A) The drawer is the creditor, and the drawee is the debtor.
In a standard business scenario, a seller (creditor) sells goods on credit to a buyer (debtor). To secure payment, the seller draws a bill of exchange on the buyer. Therefore, the drawer of the bill is the creditor, and the drawee, who is expected to pay, is the debtor. Acceptance of the bill signifies the debtor's acknowledgment of the debt.

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Oct/Nov 2012

9. Based on the format of a bill of exchange, what does the phrase "for value received" signify?
(A) The bill was issued as a gift with no underlying transaction.
(B) The bill is backed by a formal government or third-party guarantee.
(C) The bill was issued for valid consideration.
(D) The bill's stated value is expected to appreciate like an investment.

Ans :

(C) The bill was issued for valid consideration.
The phrase "for value received" is a traditional component of a bill of exchange that indicates the drawer has given some consideration to the drawee, creating the debt. This consideration is typically goods sold or services rendered on

CHAPTER 8
Bills of Exchange

Oct/Nov 2018

1. According to the objectives listed, which of the following skills will a student acquire after studying the unit on Bills of Exchange?
(A) Auditing bill transactions
(B) Preparing a bills receivable journal and bills payable journal
(C) Valuing financial derivatives
(D) Calculating foreign exchange rates

Ans :

(B) Preparing a bills receivable journal and bills payable journal
The stated objectives of the unit include enabling the student to pass entries for bill transactions and to prepare a bills receivable journal and bills payable journal. The other options, such as auditing, valuing derivatives, or calculating foreign exchange rates, are not mentioned as learning outcomes for this specific chapter on bills of exchange.

May/June 2013

2. When are separate journals, such as a bills receivable journal and a bills payable journal, typically maintained in business accounting?
(A) When transactions of a similar nature are numerous
(B) Only when the business operates as a sole proprietorship
(C) Only when the business is engaged in international trade
(D) When the business has fewer than ten transactions per month

Ans :

(A) When transactions of a similar nature are numerous
A separate journal is maintained for specific types of transactions when those transactions occur frequently. This practice, known as using special journals or subdividing the main journal, helps in organizing records efficiently. For bills of exchange, if a business engages in many such transactions, separate bills receivable and payable journals are used.

Oct/Nov 2021

3. What is the primary role of an 'Instrument of Credit' in business transactions?
(A) It serves as a primary marketing tool for new products.
(B) It functions as a detailed checklist for internal audit procedures.
(C) It acts as tangible proof that a credit agreement exists.
(D) It is a mandatory government permit required for extending credit.

Ans :

(C) It acts as tangible proof that a credit agreement exists.
In business, credit transactions are common. To formalize these arrangements, a written document called an 'Instrument of Credit' is obtained. This document, such as a bill of exchange or promissory note, provides tangible evidence of the credit agreement, specifying the terms and parties involved, thereby serving as legal proof of the debt.

May/June 2005

4. Which of the following are identified as the most commonly used instruments of credit in business?
(A) Cheques and Demand Drafts
(B) Credit Cards and Debit Cards
(C) Share Certificates and Debentures
(D) Bills of Exchange and Promissory Notes

Ans :

(D) Bills of Exchange and Promissory Notes
The text explicitly identifies two main instruments of credit that are most commonly used in business transactions to formalize credit arrangements. These are Bills of Exchange, which are orders to pay, and Promissory Notes, which are promises to pay. These instruments are central to managing

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is the total amount of capital receipts from these transactions?
(A) ₹1,260,000
(B) ₹1,200,000
(C) ₹1,250,000
(D) ₹1,000,000

Ans :

(C) ₹1,250,000
Capital receipts are from non-operating activities. The issue of shares brings in 100,000 × (₹10 + ₹2) = ₹1,200,000. The sale of a fixed asset (furniture) brings in ₹50,000. Both are capital receipts. The total capital receipt is ₹1,200,000 + ₹50,000 = ₹1,250,000. The ₹10,000 profit on furniture is a revenue item.

May/June 2023

100. According to the distinction table, what is the purpose of capital expenditure versus revenue expenditure?
(A) Capital: to enhance capacity; Revenue: to maintain assets.
(B) Capital: to maintain assets; Revenue: to enhance capacity.
(C) Both have the purpose of maintaining assets.
(D) Both have the purpose of enhancing capacity.

Ans :

(A) Capital: to enhance capacity; Revenue: to maintain assets.
The distinction table clearly states that the purpose of capital expenditure is "to improve or enhance business or productive or earning capacity." In contrast, the purpose of revenue expenditure is "to maintain the fixed assets in good working condition." This highlights the core difference in their strategic intent.

Oct/Nov 2018

101. Which of the following best describes the 'benefit from expenditure' test for classifying an expense?
(A) If the benefit is of short duration, it is revenue; if of long duration, it is capital.
(B) If the benefit is tangible, it is capital; if intangible, it is revenue.
(C) If the benefit is for the customer, it is revenue; if for the company, it is capital.
(D) If the benefit is financial, it is capital; if non-financial, it is revenue.

Ans :

(A) If the benefit is of short duration, it is revenue; if of long duration, it is capital.
This test focuses on the time period over which the economic benefits of an expenditure are expected to flow to the entity. Expenditures whose benefits are consumed within one accounting cycle are revenue. Expenditures whose benefits extend over several years are capitalized to be matched with revenues in future periods.

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May/June 2007

102. An expenditure incurred on the renewal of a patent is:
(A) A deferred revenue expenditure.
(B) A capital expenditure.
(C) A contingent liability.
(D) A revenue expenditure.

Ans :

(B) A capital expenditure.
A patent is an intangible asset. The cost to renew it extends the legal life and the period of exclusive economic benefits derived from it. Since this expenditure provides a long-term benefit beyond the current period, it is appropriately classified as a capital expenditure and added to the cost of the patent.

Oct/Nov 2025

103. Which of the following is NOT an example of capital expenditure provided in the text?
(A) Payment of employee salaries.
(B) Purchase of plant and machinery.
(C) Purchase of computer software.
(D) Purchase of patent rights.

Ans :

(A) Payment of employee salaries.
The text provides plant, machinery, computer software, and patent rights as examples of capital expenditure. Payment of employee salaries is explicitly mentioned as an example of a recurring expense, which is classified as a revenue expenditure. The exception is salaries directly related to the construction of an asset, which are capitalized.

May/June 2012

104. Consider the following two statements:
Statement I : All non-recurring expenditures are treated as capital expenditures without exception.
Statement II : The materiality concept can allow a non-recurring expenditure of a small amount to

credit. It establishes that the bill is not gratuitous but arises from a genuine business transaction.

May/June 2019

10. What is the key difference in how a bill of exchange and a promissory note are created?
(A) A bill of exchange is drawn by the creditor, while a promissory note is written by the debtor.
(B) A bill of exchange is drawn by the debtor, while a promissory note is drawn by the creditor.
(C) A bill of exchange requires a stamp, while a promissory note does not.
(D) A bill of exchange has two parties, while a promissory note has three.

Ans :

(A) A bill of exchange is drawn by the creditor, while a promissory note is written by the debtor.
A fundamental distinction lies in their origin. A bill of exchange is an order drawn by a creditor (e.g., a seller) directing a debtor (e.g., a buyer) to pay. Conversely, a promissory note is an undertaking written and signed by a debtor (maker) promising to pay a certain sum of money to a creditor (payee).

Oct/Nov 2006

11. According to Section 4 of the Negotiable Instruments Act, a promissory note is defined as an instrument containing an unconditional what?
(A) Order
(B) Request
(C) Instruction
(D) Undertaking

Ans :

(D) Undertaking
A promissory note is fundamentally a promise. Section 4 of the Negotiable Instruments Act defines it as an instrument in writing containing an unconditional undertaking, signed by the maker, to pay a certain sum of money. This distinguishes it from a bill of exchange, which contains an unconditional 'order' to pay, not an 'undertaking' or promise.

May/June 2017

12. How many parties are typically involved in a promissory note?
(A) One
(B) Two
(C) Three
(D) Four

Ans :

(B) Two
A promissory note involves only two parties. The first is the 'Maker', who is the person making the promise to pay and signing the note (the debtor). The second is the 'Payee', who is the person to whom the payment is to be made (the creditor). This contrasts with a bill of exchange, which typically has three parties.

Oct/Nov 2023

13. In the context of a promissory note, who is the 'Maker'?
(A) The person who is designated on the note to receive the money.
(B) The government authority that validates and stamps the promissory note.
(C) The party who creates the note and promises to pay.
(D) The financial institution that discounts the note for immediate cash.

Ans :

(C) The party who creates the note and promises to pay.
The 'Maker' of a promissory note is the party who creates the instrument. This person is the debtor who promises to pay a specified sum of money to another party, the payee. The maker's signature on the note is what makes the promise legally binding. The maker in a promissory note is analogous to the acceptor in a bill of exchange.

May/June 2009

14. Which statement correctly reflects a key distinction between a Bill of Exchange and a Promissory Note?
(A) A bill of exchange is made by a debtor, while a promissory note is made by a creditor.
(B) Acceptance is not required for a bill of exchange, but it is necessary for a promissory note.
(C) A bill of exchange has two parties, while a promissory note has three parties.
(D) A bill of exchange is an unconditional order to pay, while a promissory note is an unconditional promise to pay.

Ans :

NODIA

(D) To collect the payment from the drawee on the due date.

Ans :

(A) To protest negotiable instruments for dishonour.
A Notary Public is a government-appointed officer whose functions include formally certifying the dishonour of a negotiable instrument. When a bill is dishonoured, the holder can present it to a notary, who then makes entries and issues a certificate called a 'Protest', which serves as legal evidence of the dishonour.

May/June 2007

36. The process of recording the fact of dishonour on a bill by a notary public is called:
(A) Protesting
(B) Noting
(C) Discounting
(D) Endorsing

Ans :

(B) Noting
'Noting' is the act performed by a notary public upon the dishonour of a bill. The notary presents the bill for payment again, and if payment is refused, they record the fact of dishonour, the date, and the reasons given, either on the bill itself or on an attached slip. This formal act precedes protesting.

Oct/Nov 2009

37. The certificate issued by a notary public certifying the dishonour of a bill is known as a:
(A) Noting Certificate
(B) Protest
(C) Dishonour Note
(D) Bill Certificate

Ans :

(B) Protest
While noting is the act of recording the dishonour, the formal certificate issued by the notary public that details the dishonour is called a 'Protest'. This certificate is admissible in court as authentic proof that the instrument was duly presented for payment or acceptance and was dishonoured. It is a more formal step than just noting.

May/June 2023

38. What are 'Noting Charges'?
(A) The fee paid to a Notary Public for certifying a bill's dishonour.
(B) The service charge deducted by a bank for discounting a bill before maturity.
(C) The interest amount added to a new bill during the renewal process.
(D) The commission paid to a collection agent for recovering the bill amount.

Ans :

(A) The fee paid to a Notary Public for certifying a bill's dishonour.
Noting charges are the fees levied by the Notary Public for their service of formally noting and/or protesting a dishonoured bill. These charges are initially paid by the holder of the bill at the time of dishonour but are ultimately recoverable from the party responsible for the dishonour, which is typically the drawee/acceptor.

Oct/Nov 2022

39. What is the allowance given by the holder to the drawee for paying a bill before its due date called?
(A) Rebate
(B) Discount
(C) Commission
(D) Interest

Ans :

(A) Rebate
When a drawee retires a bill by paying it before the maturity date, the holder may grant an allowance or discount as an incentive for the early payment. This specific type of allowance in the context of retiring a bill is known as a 'Rebate'. It is calculated on the bill amount for the unexpired period.

May/June 2016

40. Mr. A draws a bill on B for ₹10,000. B accepts it. If A retains the bill, what is the journal entry in A's books upon receipt of the accepted bill?
(A) Dr. Bills Receivable a/c ₹10,000; Cr. B a/c ₹10,000
(B) Dr. Cash a/c ₹10,000; Cr. B a/c ₹10,000
(C) Dr. B a/c ₹10,000; Cr. Bills Payable a/c ₹10,000
(D) Dr. Sales a/c ₹10,000; Cr. B a/c ₹10,000

Ans :

(A) Dr. Bills Receivable a/c ₹10,000; Cr. B a/c ₹10,000
When A receives the accepted bill from B, the bill becomes an asset called 'Bills Receivable'. This increases the Bills Receivable account,

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May/June 2006

20. What is a key difference regarding acceptance between a bill of exchange and a cheque?
(A) A bill of exchange requires acceptance, while a cheque does not require any acceptance.
(B) A cheque requires acceptance by the drawee bank, while a bill of exchange does not.
(C) Both instruments require acceptance from the drawee.
(D) Acceptance is optional for both instruments.

Ans :

(A) A bill of exchange requires acceptance, while a cheque does not require any acceptance.
A bill of exchange requires acceptance by the drawee to become a binding liability on them. In contrast, a cheque does not require acceptance. A cheque is an order to the bank to pay on demand, and the bank either honours it or dishonours it upon presentation.

Oct/Nov 2011

21. What is the difference between a bill of exchange and a cheque concerning the drawee?
(A) A cheque can be drawn on any person, while a bill of exchange can only be drawn on a bank.
(B) Both can only be drawn on a bank.
(C) The drawee for both must be a financial institution.
(D) A bill of exchange can be drawn on any person, while a cheque can only be drawn on a bank.

Ans :

(D) A bill of exchange can be drawn on any person, while a cheque can only be drawn on a bank.
A bill of exchange can be drawn upon any person, including an individual, a firm, or a bank. However, a cheque is a specific type of bill of exchange that can only be drawn upon a bank.

May/June 2012

22. What is the rule regarding stamping for a bill of exchange versus a cheque?
(A) Both must be stamped.
(B) A bill of exchange must be stamped, while a cheque does not require any stamp.
(C) A cheque must be stamped, while a bill of exchange does not require a stamp.
(D) Stamping is optional for both, depending on the amount.

Ans :

(B) A bill of exchange must be stamped, while a cheque does not require any stamp.
A bill of exchange must be stamped according to the relevant stamp act to be legally valid. In contrast, a cheque is exempt from this requirement and does not need to be stamped, which facilitates its use in everyday banking transactions.

Oct/Nov 2025

23. What is the period of a bill of exchange called?
(A) Grace Period
(B) Maturity Period
(C) Term or Tenor
(D) Discounting Period

Ans :

(C) Term or Tenor
The period of a bill, which is the time between its drawing and its due date for payment, is referred to as its 'Term' or 'Tenor'. This period is specified on the instrument itself, for example, "two months after date." The maturity date is calculated based on this term plus any applicable grace days.

May/June 2020

24. How is the date of maturity calculated for a bill of exchange that is not payable on demand?
(A) It is the bill's date of drawing plus the exact number of days in the term.
(B) It is always the last business day of the month in which the bill's term ends.
(C) It is the date of acceptance plus the specified term, without any grace period.
(D) It is the bill's nominal due date plus three days of grace.

Ans :

(D) It is the bill's nominal due date plus three days of grace.
For any bill of exchange or promissory note not expressed to be payable on demand, at sight, or on presentment, the law allows for a grace period. The maturity date is determined by adding three days, known as 'days of grace', to the date on which the nominal term of the bill expires.

Oct/Nov 2013

25. If a bill is drawn on March 1 for a period of one month, what will be its due date?
(A) April 4

NODIA

(B) April 1
(C) April 3
(D) March 31

Ans :

(A) April 4
The term of the bill is one month, so it nominally falls due on April 1. To this date, three days of grace are added. Therefore, the legal due date, or the date of maturity, will be April 1 plus three days, which is April 4. This is the standard procedure for calculating the maturity date.

May/June 2015

26. What happens if the calculated due date of a bill of exchange falls on a public holiday?
(A) The bill becomes due on the next working day.
(B) The bill becomes due on the previous working day.
(C) The bill is considered void.
(D) The bill is payable on the public holiday itself.

Ans :

(B) The bill becomes due on the previous working day.
The Negotiable Instruments Act provides a specific rule for due dates that fall on public holidays. In such cases, the instrument is deemed to be due on the preceding business day. For example, if the due date is January 26 (a public holiday), the bill must be paid on January 25.

Oct/Nov 2020

27. Who is defined as a 'Holder' of a negotiable instrument?
(A) Any person who has temporary physical possession of the instrument.
(B) The original person who drew or created the instrument, regardless of transfers.
(C) The person legally entitled to receive the payment due.
(D) The notary public responsible for protesting the instrument upon dishonour.

Ans :

(C) The person legally entitled to receive the payment due.
The term 'Holder' has a specific legal meaning. It refers not just to physical possession but to the legal right to possess the instrument and to receive or recover the amount due thereon from the parties liable. This person has the legal standing to demand payment and give a valid discharge upon receiving it.

May/June 2018

28. Which of the following is NOT a condition for a person to be considered a 'Holder in due course'?
(A) He became the holder of the instrument after its maturity.
(B) He obtained the instrument for valuable consideration.
(C) He had no cause to believe that any defect existed in the title of the person from whom he derived his title.
(D) He became the holder of the instrument before its maturity.

Ans :

(A) He became the holder of the instrument after its maturity.
To qualify as a holder in due course, a person must become the holder of the instrument before its maturity. Acquiring the instrument after it is already overdue is one of the factors that prevents a person from gaining this privileged status. The other three options are valid conditions for being a holder in due course.

Oct/Nov 2005

29. What is the meaning of 'Honouring of bill'?
(A) The drawee accepts the bill upon presentation.
(B) The drawer discounts the bill with the bank.
(C) The drawee pays the amount of the bill on the due date.
(D) The bill is endorsed to a creditor.

Ans :

(C) The drawee pays the amount of the bill on the due date.
A bill is said to be 'honoured' or 'met' when the party liable to pay (the drawee or acceptor) makes the full payment of the amount specified in the bill on its maturity date. This action successfully concludes the transaction, and the liability of the acceptor is discharged.

May/June 2021

30. What does the term 'Discounting of bill' refer to?
(A) En cashing the bill with a bank before its maturity date.
(B) The drawee paying a penalty for settling the bill after the due date.
(C) The drawer agreeing to accept a reduced payment from the drawee as a final

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settlement.
(D) The formal cancellation of a bill by mutual agreement of all parties involved.

Ans :

(A) Encashing the bill with a bank before its maturity date.
Discounting is a facility that allows the holder of a bill to get its value before the maturity date. The holder endorses the bill to a banker, who pays the holder the face value of the bill less a small charge (discount). The bank then collects the full amount from the drawee on the due date.

Oct/Nov 2019

31. What is the 'Endorsement of bill'?
(A) The process of the drawee signing the bill for acceptance.
(B) The act of paying the bill amount on the due date.
(C) The cancellation of the bill by mutual consent.
(D) The transfer of a bill to some other person by the holder.

Ans :

(D) The transfer of a bill to some other person by the holder.
Endorsement is the act of the holder of a negotiable instrument signing it, usually on the back, to transfer their rights to another person. This action transfers the title of the bill to the new holder (the endorsee), who then becomes entitled to receive the payment on the due date.

May/June 2024

32. The event where a drawee pays the bill before its due date is known as:
(A) Honouring of bill
(B) Retirement of bill
(C) Renewal of bill
(D) Dishonour of bill

Ans :

(B) Retirement of bill
'Retirement of bill' refers to the specific situation where the drawee (acceptor) makes the payment for the bill before its scheduled maturity date. Often, the holder may give a small discount, known as a 'rebate', to the drawee for this early payment. This is different from honouring, which happens on the due date.

Oct/Nov 2017

33. What is a 'Renewal of bill'?
(A) The drawee making the full payment on the exact maturity date.
(B) The holder selling the bill to a bank for cash before its maturity.
(C) Cancelling an old bill and drawing a new one for an extended term.
(D) The formal transfer of the bill's title from the holder to a new creditor.

Ans :

(C) Cancelling an old bill and drawing a new one for an extended term.
When a drawee is unable to pay the bill on its due date, they may request the drawer to cancel the original bill and draw a new one for a fresh period. This process is called renewal. Often, the drawee pays a portion of the amount in cash and is charged interest on the balance for the extended credit period.

May/June 2008

34. An 'Accommodation bill' is one where:
(A) A bill is drawn specifically to finance a documented sale of goods or services.
(B) A bill is drawn without consideration for mutual financial assistance.
(C) A bill is drawn for an unusually long period, such as more than one year.
(D) A bill has been formally accepted by a commercial bank (a "banker's acceptance").

Ans :

(B) A bill is drawn without consideration for mutual financial assistance.
Unlike a trade bill, which arises from a genuine trade transaction (consideration), an accommodation bill is drawn and accepted without any underlying sale or purchase. Its sole purpose is to provide financial assistance to one or both parties by getting the bill discounted from a bank to raise funds.

Oct/Nov 2007

35. What is the primary function of a Notary Public in relation to negotiable instruments?
(A) To protest negotiable instruments for dishonour.
(B) To discount the bill of exchange for the holder.
(C) To draw the bill of exchange on behalf of the creditor.

NODIA

(A) Dr. Cash a/c; Cr. Bills Receivable a/c
On the due date, the drawer receives cash from the drawee. This increases the cash balance, so Cash a/c is debited. The asset 'Bills Receivable' is now realized, so the Bills Receivable account is credited to close it. This entry reflects the conversion of the bill into cash upon its honour.

May/June 2007

46. What entry is made in the drawer's books when a discounted bill is met on the due date?
(A) Dr. Cash a/c; Cr. Bills Receivable a/c
(B) No Entry
(C) Dr. B's a/c; Cr. Bank a/c
(D) Dr. Bank a/c; Cr. B's a/c

Ans :

(B) No Entry
When a discounted bill is met, the drawee pays the amount directly to the bank that discounted the bill. Since the drawer has already received the money (less discount) from the bank at the time of discounting, there is no further transaction involving the drawer. Therefore, no entry is required in the drawer's books.

Oct/Nov 2023

47. When a bill sent for collection is honoured and the bank remits the money, what is the entry in the drawer's books?
(A) Dr. Cash or Bank a/c; Cr. Bills Receivable a/c
(B) Dr. B's a/c; Cr. Bank for Bill Collection a/c
(C) No Entry
(D) Dr. Cash or Bank a/c; Cr. Bank for Bill Collection a/c

Ans :

(D) Dr. Cash or Bank a/c; Cr. Bank for Bill Collection a/c
When the bill was sent for collection, the 'Bank for Bill Collection' account was debited. Now that the bank has collected the money and remitted it, the drawer's cash/bank balance increases (debited), and the temporary 'Bank for Bill Collection' account is closed by crediting it.

May/June 2014

48. When a bill is honoured on the due date, what is the journal entry in the drawee's books, regardless of how the drawer used the bill?
(A) Dr. Bills Payable a/c; Cr. Cash/Bank a/c
(B) Dr. A's a/c; Cr. Cash/Bank a/c
(C) Dr. Bills Receivable a/c; Cr. Cash/Bank a/c
(D) No Entry

Ans :

(A) Dr. Bills Payable a/c; Cr. Cash/Bank a/c
On the due date, the drawee pays the bill. This payment discharges the liability recorded as 'Bills Payable', so the Bills Payable account is debited. The payment is made in cash or through the bank, so the Cash/Bank account is credited. This entry remains the same regardless of who presents the bill for payment.

Oct/Nov 2012

49. What is an advantage of 'noting' a dishonoured bill?
(A) It automatically renews the bill for a further period.
(B) It waives the need for the drawee to pay.
(C) It secures evidence of the dishonour.
(D) It reduces the amount payable by the drawee.

Ans :

(C) It secures evidence of the dishonour.
The primary advantage of having a bill noted by a notary public is that it creates an authentic, official record of the fact that the bill was presented for payment and was dishonoured. This formal evidence can be crucial if legal action is required to recover the amount from the liable parties.

May/June 2005

50. A bill for ₹10,000 retained by drawer A is dis honoured, and A pays ₹100 as noting charges. What is the journal entry in A's books?
(A) Dr. B's a/c ₹10,100; Cr. Bills Receivable a/c ₹10,000; Cr. Cash a/c ₹100
(B) Dr. B's a/c ₹10,000; Cr. Bills Receivable a/c ₹10,000
(C) Dr. Bills Receivable a/c ₹10,100; Cr. B's a/c ₹10,100
(D) Dr. B's a/c ₹10,100; Cr. Cash a/c ₹10,100

Ans :

(A) Dr. B's a/c ₹10,100; Cr. Bills Receivable a/c ₹10,000; Cr. Cash a/c ₹100
Upon dishonor, the bill is no longer a valid asset, so Bills Receivable is credited with ₹10,000. A pays ₹100 cash for noting, so Cash is credited. The total amount, including noting charges (₹10,100), is now recoverable from the drawee B, making B a debtor again. Therefore, B's account is debited for the total amount due.

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which is debited. The bill is received from B, who was a debtor. The receipt of the bill converts the personal debtor into a bill, so B's account is credited to close the receivable.

Oct/Nov 2014

41. A discounts a bill of ₹10,000 with his bank for ₹9,800. What is the correct journal entry in the books of A (the drawer)?

(A) Dr. Cash a/c ₹10,000; Cr. Bills Receivable a/c ₹10,000

(B) Dr. Bank a/c ₹9,800; Cr. Bills Receivable a/c ₹9,800

(C) Dr. Cash a/c ₹9,800; Dr. Discount a/c ₹200; Cr. B's a/c ₹10,000

(D) Dr. Cash a/c ₹9,800; Dr. Discount a/c ₹200; Cr. Bills Receivable a/c ₹10,000

Ans :

(D) Dr. Cash a/c ₹9,800; Dr. Discount a/c ₹200; Cr. Bills Receivable a/c ₹10,000

A receives cash of ₹9,800, so Cash a/c is debited. The difference of ₹200 between the face value and cash received is an expense (discount), so Discount a/c is debited. The asset 'Bills Receivable' of ₹10,000 is no longer with A, so the Bills Receivable a/c is credited to remove it from the books.

May/June 2010

42. If A endorses a bill of ₹10,000 to his creditor, C, what journal entry is passed in A's books?

(A) Dr. Bills Receivable a/c ₹10,000; Cr. C's a/c ₹10,000

(B) Dr. C's a/c ₹10,000; Cr. Bills Receivable a/c ₹10,000

(C) Dr. C's a/c ₹10,000; Cr. Bills Payable a/c ₹10,000

(D) Dr. B's a/c ₹10,000; Cr. C's a/c ₹10,000

Ans :

(B) Dr. C's a/c ₹10,000; Cr. Bills Receivable a/c ₹10,000

By endorsing the bill to C, A settles a liability. Therefore, the creditor's account (C's a/c) is debited to reduce the liability. The asset, 'Bills Receivable', is given away, so the Bills Receivable account is credited. This entry reflects the settlement of a liability using the bill as a form of payment.

Oct/Nov 2009

43. What is the journal entry in the books of B (the drawee) when he accepts a bill of ₹10,000 drawn by A?

(A) Dr. Bills Payable a/c ₹10,000; Cr. A's a/c ₹10,000

(B) Dr. Purchases a/c ₹10,000; Cr. Bills Payable a/c ₹10,000

(C) Dr. A's a/c ₹10,000; Cr. Bills Payable a/c ₹10,000

(D) Dr. A's a/c ₹10,000; Cr. Cash a/c ₹10,000

Ans :

(C) Dr. A's a/c ₹10,000; Cr. Bills Payable a/c ₹10,000

When B accepts the bill, his liability to A (a creditor) is converted into a formal liability known as 'Bills Payable'. Therefore, A's account is debited to cancel the personal liability, and the Bills Payable account is credited to recognize the new, formal liability under the accepted bill.

May/June 2021

44. In the books of B (the drawee), what entry is passed when the drawer (A) discounts the bill, sends it for collection, or endorses it?

(A) A separate entry is passed for each action.

(B) B's a/c is debited and Bills Payable a/c is credited.

(C) Bills Payable a/c is debited and Cash a/c is credited.

(D) No entry will be passed.

Ans :

(D) No entry will be passed.

The actions of discounting, sending for collection, or endorsing the bill are transactions between the holder (drawer) and third parties. These actions do not involve the drawee (B). The drawee's liability remains the same: to pay the bill on the due date to whoever presents it. Therefore, B makes no entry for these events.

Oct/Nov 2015

45. When a bill retained by the drawer is met on the due date, what entry is passed in the drawer's books?

(A) Dr. Cash a/c; Cr. Bills Receivable a/c

(B) Dr. B's a/c; Cr. Bills Receivable a/c

(C) Dr. Cash a/c; Cr. B's a/c

(D) Dr. Bills Payable a/c; Cr. Cash a/c

Ans :

NODIA

'Bills Receivable' with a face value of ₹10,000 is now settled and must be removed from the books (Credit Bills Receivable a/c).

May/June 2017

56. What is the journal entry in the drawee's (Suresh's) books for the retirement of the bill for ₹9,500?

(A) Dr. Bills Payable a/c ₹10,000; Cr. Cash a/c ₹10,000
(B) Dr. Bills Payable a/c ₹10,000; Cr. Cash a/c ₹9,500; Cr. Rebate a/c ₹500
(C) Dr. Bills Payable a/c ₹9,500; Dr. Rebate a/c ₹500; Cr. Cash a/c ₹10,000
(D) Dr. Cash a/c ₹9,500; Dr. Rebate a/c ₹500; Cr. Bills Payable a/c ₹10,000

Ans :

(B) Dr. Bills Payable a/c ₹10,000; Cr. Cash a/c ₹9,500; Cr. Rebate a/c ₹500
Suresh settles his liability of 'Bills Payable' worth ₹10,000 (Debit Bills Payable a/c). He pays ₹9,500 in cash (Credit Cash a/c). The ₹500 difference is a gain or income for him, known as rebate (Credit Rebate a/c). This entry correctly reflects the discharge of the liability and the income earned from early payment.

Oct/Nov 2005

57. When a bill is renewed, what is the first accounting step that must be taken in the books of both parties?

(A) Calculate interest for the new period.
(B) Draw the new bill.
(C) Receive part payment in cash.
(D) The old bill must be cancelled.

Ans :

(D) The old bill must be cancelled.
The process of renewal begins with the cancellation of the original bill. This is because the original bill represents a liability that will not be met on its due date. Cancelling it reverses the initial entry, typically by debiting the drawee and crediting Bills Receivable in the drawer's books, and debiting Bills Payable and crediting the drawer in the drawee's books.

May/June 2020

58. Suresh requests renewal of a ₹10,000 bill. He pays ₹4,000 cash and accepts a new bill for the balance plus interest. How much is the interest charged by Ramesh for 3 months at 10 % per annum?

(A) ₹150
(B) ₹100
(C) ₹200
(D) ₹250

Ans :

(A) ₹150
The original bill amount is ₹10,000. Suresh pays ₹4,000, leaving a balance of ₹6,000. Interest is calculated on this balance for the new credit period. The calculation is:
Interest = Principal × Rate × Time

$$= 6{,}000 \times \frac{10}{100} \times \frac{3}{12}$$

$$= ₹150.$$

This interest amount will be added to the new bill.

Oct/Nov 2015

59. Following the previous question, what will be the amount of the new bill drawn by Ramesh on Suresh?

(A) ₹6,000
(B) ₹4,000
(C) ₹6,150
(D) ₹10,150

Ans :

(C) ₹6,150
The amount of the new bill will be the outstanding balance of the old bill plus the interest charged for the extended period. The balance amount is ₹6,000 (₹10,000 - ₹4,000). The interest calculated is ₹150. Therefore, the new bill will be drawn for ₹6,000 + ₹150 = ₹6,150.

May/June 2013

60. What is the journal entry in the drawee's (Suresh's) books for the cancellation of the old bill of ₹10,000 during renewal?

(A) Dr. Bills Payable a/c ₹10,000; Cr. Ramesh a/c ₹10,000
(B) Dr. Ramesh a/c ₹10,000; Cr. Bills Payable a/c ₹10,000
(C) Dr. Bills Payable a/c ₹10,000; Cr. Cash a/c ₹10,000
(D) Dr. Bills Payable a/c ₹10,000; Cr. Interest a/c ₹10,000

Ans :

(A) Dr. Bills Payable a/c ₹10,000; Cr. Ramesh a/c ₹10,000

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Oct/Nov 2025

51. If a discounted bill of ₹10,000 is dishonoured and the bank pays ₹100 in noting charges, what is the journal entry in the drawer's books to make the drawee liable for the full amount?

(A) Dr. Bills Receivable a/c ₹10,000; Dr. Noting Charges a/c ₹100; Cr. B's a/c ₹10,100
(B) Dr. B's a/c ₹10,100; Cr. Bills Receivable a/c ₹10,000; Cr. Noting Charges a/c ₹100
(C) Dr. Bank a/c ₹10,100; Cr. B's a/c ₹10,100
(D) Dr. B's a/c ₹10,100; Cr. Bank a/c ₹10,100

Ans :

(D) Dr. B's a/c ₹10,100; Cr. Bank a/c ₹10,100
When a discounted bill is dishonoured, the bank debits the drawer's account for the full amount of the bill plus any noting charges it paid. The drawer, in turn, must make the drawee liable for this total amount. The most direct entry is to debit the drawee's account (B's a/c) for ₹10,100 and credit the Bank a/c to reflect the amount paid back to the bank.

May/June 2008

52. When an endorsed bill is dishonoured, the endorsee (C) pays noting charges. What is the entry in the original drawer's (A's) books to record the receipt of the dishonoured bill back from C?

(A) Dr. B's a/c ₹10,100; Cr. C's a/c ₹10,100
(B) Dr. Bill Receivable a/c ₹10,000; Dr. Noting Charges a/c ₹100; Cr. C's a/c ₹10,100
(C) Dr. C's a/c ₹10,100; Cr. Bills Receivable a/c ₹10,000; Cr. Noting Charges a/c ₹100
(D) Dr. B's a/c ₹10,100; Cr. Bills Receivable a/c ₹10,000; Cr. Noting Charges a/c ₹100

Ans :

(B) Dr. Bill Receivable a/c ₹10,000; Dr. Noting Charges a/c ₹100; Cr. C's a/c ₹10,100
When the endorsed bill is dishonoured, the drawer (A) becomes liable to the endorsee (C) for the bill amount plus noting charges. C's account is credited for ₹10,100 to show this liability. A gets the bill back, so Bills Receivable is debited (₹10,000), and the Noting Charges paid by C are also recorded as a debit.

Oct/Nov 2011

53. In all cases of dishonour, what is the journal entry passed in the books of the drawee (B)?

(A) Dr. A's a/c ₹10,100; Cr. Bills Payable ₹10,000; Cr. Noting Charges ₹100
(B) Dr. Bills Payable ₹10,100; Cr. Cash a/c ₹10,100
(C) Dr. Bills Payable ₹10,000; Dr. Noting Charges ₹100; Cr. A's a/c ₹10,100
(D) No entry is passed in the drawee's books.

Ans :

(C) Dr. Bills Payable a/c ₹10,000; Dr. Noting Charges a/c ₹100; Cr. A's a/c ₹10,100
Upon dishonour, the drawee's (B's) liability under 'Bills Payable' is cancelled, so Bills Payable is debited (₹10,000). The noting charges are an expense for B, so Noting Charges is debited (₹100). The total amount is now owed back to the original drawer (A), re-establishing A as a creditor, so A's account is credited for ₹10,100.

May/June 2010

54. Suresh retires a bill of ₹10,000 drawn by Ramesh by paying ₹9,500. What is the rebate allowed by Ramesh?

(A) ₹9,500
(B) ₹10,000
(C) Cannot be determined
(D) ₹500

Ans :

(D) ₹500
Retirement of a bill means paying it before the due date. The difference between the face value of the bill (₹10,000) and the amount paid by the drawee (₹9,500) is the rebate. In this case, the rebate is ₹10,000 - ₹9,500 = ₹500. This is an expense for the drawer (Ramesh) and income for the drawee (Suresh).

Oct/Nov 2024

55. What is the journal entry in the drawer's (Ramesh's) books for the retirement of the bill mentioned in the previous question?

(A) Dr. Cash a/c ₹9,500; Dr. Rebate a/c ₹500; Cr. Bills Receivable a/c ₹10,000
(B) Dr. Cash a/c ₹9,500; Cr. Bills Receivable a/c ₹9,500
(C) Dr. Cash a/c ₹10,000; Cr. Bills Receivable a/c ₹9,500; Cr. Rebate a/c ₹500
(D) Dr. Bills Receivable a/c ₹10,000; Cr. Cash a/c ₹9,500; Cr. Rebate a/c ₹500

Ans :

(A) Dr. Cash a/c ₹9,500; Dr. Rebate a/c ₹500; Cr. Bills Receivable a/c ₹10,000
Ramesh receives ₹9,500 in cash (Debit Cash a/c). He allows a rebate of ₹500, which is an expense for him (Debit Rebate a/c). The asset

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(D) A bill of exchange is an unconditional order to pay, while a promissory note is an unconditional promise to pay.
A primary point of distinction is that a bill of exchange is an unconditional order to pay, whereas a promissory note is an unconditional promise (or undertaking) to pay. The other options misrepresent key differences, such as reversing the roles of debtor/creditor or the number of parties involved.

Oct/Nov 2015

15. Which of the following statements about a promissory note is incorrect?
(A) Noting is necessary upon its dishonour.
(B) It is made by a debtor.
(C) No acceptance is required.
(D) There are two parties to it.

Ans :

(A) Noting is necessary upon its dishonour.
Noting by a notary public is a procedure usually associated with the dishonour of a bill of exchange to serve as formal evidence. For a promissory note, noting is not a necessary legal step upon dishonour. The other statements are all correct characteristics of a promissory note.

May/June 2022

16. For accounting purposes, how are bills of exchange and promissory notes treated?
(A) They are treated as distinct types of assets and liabilities.
(B) No distinction is made between them.
(C) Bills of exchange are current assets, while promissory notes are non-current assets.
(D) Promissory notes are recorded, but bills of exchange are not.

Ans :

(B) No distinction is made between them.
From an accounting perspective, both a bill of exchange and a promissory note represent a right to receive or an obligation to pay money. Therefore, no distinction is made between them in the books of accounts. An instrument received is treated as a 'Bill Receivable' and an instrument issued is treated as a 'Bill Payable'.

Oct/Nov 2008

17. How is a bill classified from the perspective of the drawer who is entitled to receive money?
(A) It is classified as Bills Payable.
(B) It is classified as Bills Receivable.
(C) It is classified as a contingent liability.
(D) It is classified as a deferred expense.

Ans :

(B) It is classified as Bills Receivable.
For the person who draws the bill and is set to receive the payment (the creditor or drawer), the bill represents a future economic benefit. Therefore, it is considered an asset in their books of accounts and is recorded under the head 'Bills Receivable'. This account tracks all amounts due from debtors through such instruments.

May/June 2014

18. According to Section 6 of the Negotiable Instruments Act, a cheque is defined as a bill of exchange drawn upon whom?
(A) A specified banker
(B) Any person or business entity
(C) The government treasury
(D) Another creditor

Ans :

(A) A specified banker
A key feature that distinguishes a cheque from other bills of exchange is its drawee. Section 6 of the Negotiable Instruments Act specifically defines a cheque as a bill of exchange that is drawn on a specified banker and is payable on demand. The drawee in the case of a cheque must always be a bank.

Oct/Nov 2024

19. Which of the following is NOT an essential feature of a cheque?
(A) It must be payable on demand.
(B) It must fulfill all essential elements of a bill of exchange.
(C) It must be payable only to a specific person and not to the bearer.
(D) The signature must tally with the specimen signature kept in the bank.

Ans :

(C) It must be payable only to a specific person and not to the bearer.
A cheque must be payable to bearer or to order, but in either case, it must be payable on demand. This means it can be made out to a specific person (order) or to whoever holds it (bearer). The option suggesting it can only be payable to a specific person is incorrect.

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To cancel the old bill, the 'Bills Payable' liability account is debited to eliminate it. The liability is transferred back to the personal account of the drawer, Ramesh, re-establishing him as a creditor. Therefore, Ramesh's account is credited. This entry reverses the acceptance entry.

Oct/Nov 2021

61. On June 1, 2022, Bimal draws three bills on Chetan for ₹14,000, ₹16,000, and ₹18,000. What is the consolidated journal entry in Bimal's books for the receipt of these accepted bills?

(A) Dr. Chetan a/c ₹48,000; Cr. Bills Receivable a/c ₹48,000
(B) Dr. Cash a/c ₹48,000; Cr. Chetan a/c ₹48,000
(C) Dr. Bills Receivable a/c ₹48,000; Cr. Sales a/c ₹48,000
(D) Dr. Bills Receivable No. 1 ₹14,000; Dr. Bills Receivable No. 2 ₹16,000; Dr. Bills Receivable No. 3 ₹18,000; Cr. Chetan a/c ₹48,000

Ans :

(D) Dr. Bills Receivable No. 1 ₹14,000; Dr. Bills Receivable No. 2 ₹16,000; Dr. Bills Receivable No. 3 ₹18,000; Cr. Chetan a/c ₹48,000
When Bimal receives the three accepted bills, his assets in the form of Bills Receivable increase. While a single Bills Receivable account can be debited for the total, it is better practice to debit each bill individually to maintain separate records, especially when they have different due dates. Chetan, the debtor, is credited for the total amount of ₹48,000, as his personal debt is now converted into bills.

May/June 2024

62. Bimal discounts a bill (face value ₹16,000) for ₹15,900. What is the amount of discount recorded in Bimal's books?

(A) ₹16,000
(B) ₹100
(C) ₹15,900
(D) ₹240

Ans :

(B) ₹100
The discount is the difference between the face value of the bill and the cash received from the bank. The face value is ₹16,000 and the cash received is ₹15,900. Therefore, the discount expense recorded by Bimal is ₹16,000 - 15,900 = ₹100. This is recorded as a debit to the Discount account.

Oct/Nov 2008

63. A bill for ₹16,000 is dishonoured, and noting charges are ₹240. What is the total amount that the drawee (Chetan) becomes liable for to the drawer (Bimal)?

(A) ₹16,000
(B) ₹15,900
(C) ₹16,240
(D) ₹16,300

Ans :

(C) ₹16,240
When the bill is dishonoured, the drawee (Chetan) becomes liable not only for the original face value of the bill but also for any noting charges paid by the holder. Therefore, Chetan's liability to Bimal is the bill amount of ₹16,000 plus the noting charges of ₹240, totaling ₹16,240.

May/June 2006

64. Following a dishonour, Bimal charges Chetan ₹300 for interest and draws a new bill. The amount due from the dishonoured bill plus noting charges was ₹16,240. What is the amount of this new bill?

(A) ₹16,240
(B) ₹16,300
(C) ₹16,000
(D) ₹16,540

Ans :

(D) ₹16,540
The amount due from Chetan after the dishonour of the second bill was ₹16,240 (₹16,000 bill + ₹240 noting charges). Bimal then charges an additional ₹300 as interest. The new bill is drawn for the total amount due, which is ₹16,240 + ₹300 = ₹16,540.

Oct/Nov 2017

65. A drawer records the dishonour of a discounted bill, charges interest, and draws a new bill. Which statement accurately describes the series of journal entries on the drawer's books?

(A) The drawer records liability to the bank, makes the drawee liable, charges interest, and draws a new bill.
(B) The drawer receives payment for the second bill and draws a new bill on the drawee.
(C) The drawer pays noting charges for the third bill and receives interest from the drawee.
(D) The drawer renews the first bill and discounts the fourth bill simultaneously.

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exempt.

(D) Trade bills are drawn by the buyers of goods, while accommodation bills are drawn by the sellers.

Ans :

(A) Trade bills involve consideration, while accommodation bills do not.

A trade bill is drawn by a seller (creditor) on a buyer (debtor) to finance an actual transaction of goods. In contrast, an accommodation bill is drawn and accepted without any underlying trade transaction or consideration. Its sole purpose is to raise funds for one or both parties through discounting.

May/June 2019

76. In the case of an accommodation bill, how is the discount loss typically shared between the drawer and the drawee?

(A) The drawer, as the initiator, bears the entire discount loss.

(B) It is shared in the same ratio as the bill's proceeds.

(C) The drawee, as the accommodated party, bears the entire discount loss.

(D) It is always shared equally between the parties, regardless of how proceeds are split.

Ans :

(B) It is shared in the same ratio as the bill's proceeds.

A key principle in accounting for accommodation bills is that the cost of accommodation, which is the discount on the bill, should be borne by the parties equitably. The established practice is to share this discount expense in the same ratio as the parties shared the cash proceeds obtained from discounting the bill.

Oct/Nov 2012

77. X draws an accommodation bill on Y for ₹10,000 and discounts it for ₹9,600. X remits half the proceeds to Y. How much cash does Y receive from X?

(A) ₹5,000

(B) ₹9,600

(C) ₹4,500

(D) ₹4,800

Ans :

(D) ₹4,800

The proceeds from discounting the bill are the cash received from the bank, which is ₹9,600. X remits half of these proceeds to Y. Therefore, the amount of cash Y receives is ₹9,600 / 2 = ₹4,800. The remaining ₹4,800 is retained by X.

May/June 2011

78. Following the previous question, how much of the ₹400 discount on the first bill will be borne by Y?

(A) ₹200

(B) ₹400

(C) ₹0

(D) ₹100

Ans :

(A) ₹200

The total discount on the bill is ₹400 (₹10,000 - ₹9,600). Since the proceeds were shared equally (half each), the discount loss must also be shared equally. Therefore, Y's share of the discount is ₹400 / 2 = ₹200.

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Oct/Nov 2016

79. Y draws an accommodation bill on X for ₹9,000 and discounts it for ₹8,700. Y remits one-third of the proceeds to X. How much cash does X receive from Y?

(A) ₹3,000

(B) ₹8,700

(C) ₹2,900

(D) ₹9,000

Ans :

(C) ₹2,900

The proceeds from Y discounting his bill are ₹8,700. Y remits one-third of this amount to X.

The cash received by X is

$$\frac{1}{3} \times 8,700 = 2,900.$$

May/June 2025

80. Following the previous question, how much of the ₹300 discount on the second bill will be borne by X?

(A) ₹100

(B) ₹300

(C) ₹200

(D) ₹0

Ans :

(A) ₹100

The total discount on the second bill is ₹300 (₹9,000 - ₹8,700). Since X received one-third of

(A) ₹3,500
(B) ₹3,300
(C) ₹3,100
(D) ₹5,300

Ans :

(A) ₹3,500
When the bill for ₹3,300 is dishonoured, the drawee becomes liable for its face value. Additionally, the holder pays ₹200 in noting charges, which is also recoverable from the drawee. Thus, the total amount due from the drawee becomes the bill amount plus the new noting charges: ₹3,300 + ₹200 = ₹3,500.

Oct/Nov 2022

71. A drawee becomes bankrupt, and her estate pays a dividend of 50 paise in a rupee. If the total amount due was ₹3,500, how much cash does the holder receive?
(A) ₹3,500
(B) ₹2,550
(C) ₹1,650
(D) ₹1,750

Ans :

(D) ₹1,750
A dividend of 50 paise in a rupee means 50 % of the total debt is recovered. Therefore, the cash received by the holder is 50% of ₹3,500, which equals ₹1,750. The remaining amount will be written off as a bad debt.

May/June 2016

72. What is the amount of Bad Debts recorded by the holder upon the final settlement from the bankrupt drawee's estate in the previous question?
(A) ₹3,500
(B) ₹1,750
(C) ₹5,100
(D) ₹200

Ans :

(B) ₹1,750
The total debt was ₹3,500, and the holder received ₹1,750. The unrecoverable portion of the debt is treated as a bad debt. This amount is calculated as Total Due - Amount Received = ₹3,500 - ₹1,750 = ₹1,750. This is recorded by debiting the Bad Debts account.

Oct/Nov 2014

73. A bill for ₹5,000 is dishonoured with noting charges of ₹100. What is the journal entry in the drawee's books to record this?
(A) Dr. Drawer's a/c ₹5,100; Cr. Bills Payable ₹5,000; Cr. Noting Charges ₹100
(B) Dr. Bills Payable ₹5,100; Cr. Drawer's a/c ₹5,100
(C) Dr. Bills Payable ₹5,000; Dr. Noting Charges ₹100; Cr. Drawer's a/c ₹5,100
(D) Dr. Drawer's a/c ₹5,100; Cr. Cash a/c ₹5,100

Ans :

(C) Dr. Bills Payable ₹5,000; Dr. Noting Charges ₹100; Cr. Drawer's a/c ₹5,100
Upon dishonour, the drawee's liability under 'Bills Payable' is cancelled (Debit ₹5,000). The noting charges of ₹100 become an expense for the drawee (Debit Noting Charges). The total amount of ₹5,100 is now owed to the drawer, making them a creditor again (Credit Drawer's a/c).

May/June 2010

74. In the books of a bankrupt person, what does the 'Deficiency' account represent in the final settlement entry?
(A) The profit made by the bankrupt person.
(B) The total cash paid to all creditors.
(C) The total interest charged by creditors.
(D) The portion of debts that remains unpaid due to bankruptcy.

Ans :

(D) The portion of debts that remains unpaid due to bankruptcy.
In the context of insolvency, the Deficiency account is used to record the portion of liabilities that the insolvent person's estate cannot pay. In the final entry, liabilities are settled by paying some cash and transferring the unpaid balance to the Deficiency account, effectively writing it off.

Oct/Nov 2006

75. What is the primary distinction between a trade bill and an accommodation bill?
(A) Trade bills involve consideration, while accommodation bills do not.
(B) Trade bills are for short periods (e.g., 90 days), while accommodation bills are for long periods (e.g., over a year).
(C) Trade bills require a specific government stamp, while accommodation bills are

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its debtors. It helps in systematically tracking all such instruments, their due dates, and amounts.

May/June 2020

86. How are entries from the Bills Receivable Book posted to the ledger?

(A) Each entry is individually debited to the Bills Receivable account in the general ledger.
(B) The periodic total is posted as a single credit to the main Sales account.
(C) Debit individual customer accounts and credit the Bills Receivable account total.
(D) Credit individual customer accounts and debit the Bills Receivable account total.

Ans :

(D) Credit individual customer accounts and debit the Bills Receivable account total.
For each bill recorded, the personal account of the customer (debtor) from whom the bill is received is credited. At the end of a period (e.g., a month), the total amount of the Bills Receivable Book is posted as a single debit to the Bills Receivable account in the general ledger.

Oct/Nov 2013

87. Based on the standard format of a Bills Receivable Book, which of the following details is NOT a column?

(A) From Whom Received
(B) Date of Bill
(C) Due Date
(D) Discount Charges

Ans :

(D) Discount Charges
The standard format for a Bills Receivable Book includes columns for tracking the bill's details like origin, term, and due date. It does not have a specific column for recording discount charges, as discounting is a subsequent action and its accounting entry is made separately in the cash book and general journal.

May/June 2015

88. What is the primary purpose of a Bills Payable Book?

(A) To record details of all bills accepted in favour of creditors.
(B) To record all bills of exchange drawn by the business on its debtors.
(C) To serve as a subsidiary ledger for individual supplier accounts.
(D) To track all cash payments made against outstanding bills payable.

Ans :

(A) To record details of all bills accepted in favour of creditors.
The Bills Payable Book is a special journal used to record the details of all bills of exchange and promissory notes that a business accepts or issues, making itself liable to pay the amount to its creditors. It helps in managing and tracking these liabilities and their respective due dates.

Oct/Nov 2020

89. How are entries from the Bills Payable Book posted to the ledger?

(A) Credit individual creditor accounts and debit the Bills Payable account total.
(B) Each entry is individually credited to the Bills Payable account in the general ledger.
(C) Debit individual creditor accounts and credit the Bills Payable account total.
(D) The periodic total is posted as a single debit to the main Purchases account.

Ans :

(C) Debit individual creditor accounts and credit the Bills Payable account total.
For each bill accepted, the personal account of the creditor (drawer) is debited. At the end of a period, the total amount of bills accepted during that period is posted in one lump sum to the credit of the Bills Payable account in the general ledger.

May/June 2018

90. In the 'Drawn by' column of a Bills Payable Book, which party is listed?

(A) The creditor who drew the bill on the business.
(B) The business itself (the acceptor).
(C) The bank where the bill is payable.
(D) The payee of the bill.

Ans :

(A) The creditor who drew the bill on the business.
In the Bills Payable Book, the business is the acceptor or drawee. The 'Drawn by' column is used to record the name of the person or entity that created the bill and to whom the business owes money. This party is the creditor, also known as the drawer of the bill.

NODIA

the proceeds, X must also bear one-third of the discount cost.
Therefore, X's share of the discount is

$$\frac{1}{3} \times 300 = 100.$$

Oct/Nov 2010

81. Y becomes insolvent, and X has to honour his acceptance of a ₹9,000 bill. Before that, a ₹10,000 bill drawn by X on Y is dishonoured. What entry does X pass for the dishonour of the ₹10,000 bill?
(A) Dr. Bank a/c ₹10,000; Cr. Y's a/c ₹10,000
(B) Dr. Y's a/c ₹10,000; Cr. Bills Receivable a/c ₹10,000
(C) Dr. Bills Payable a/c ₹10,000; Cr. Bank a/c ₹10,000
(D) Dr. Y's a/c ₹10,000; Cr. Bank a/c ₹10,000

Ans :

(D) Dr. Y's a/c ₹10,000; Cr. Bank a/c ₹10,000
The first bill was discounted by X. On the due date, Y fails to pay the bank. As the drawer, X is liable to the bank for the full amount. The bank will debit X's account. Therefore, X credits the Bank account. The amount is now recoverable from Y, so Y's account is debited for ₹10,000.

May/June 2005

82. In an accommodation bill scenario, Y's account in X's ledger shows total debits of ₹24,000 and total credits of ₹13,000. What is the final amount due from Y before insolvency settlement?
(A) ₹10,000
(B) ₹11,000
(C) ₹9,000
(D) ₹24,000

Ans :

(B) ₹11,000
The balance due is the difference between the total debits and total credits in Y's account. The balance due is ₹24,000 - ₹13,000 = ₹11,000. This is the amount on which the insolvency settlement will be calculated.

Oct/Nov 2014

83. The total amount due from an insolvent party (Y) is ₹11,000. Y's estate pays 50 % of the amount due. How much is the final amount of Bad Debts recorded in the creditor's (X's) books?
(A) ₹11,000
(B) ₹4,500
(C) ₹5,500
(D) ₹5,000

Ans :

(C) ₹5,500
The total amount due from Y is ₹11,000. Since Y's estate pays 50 % (₹5,500), the remaining 50% is unrecoverable. This amount, ₹5,500, is therefore written off as a bad debt by debiting the Bad Debts account.

May/June 2012

84. In an accommodation bill arrangement, Y receives half the proceeds of a bill drawn by X. The cash received is ₹4,800 and Y's share of discount is ₹200. What is the journal entry in Y's books?
(A) Dr. X a/c ₹5,000; Cr. Cash a/c ₹4,800; Cr. Discount a/c ₹200
(B) Dr. Cash a/c ₹5,000; Cr. X a/c ₹5,000
(C) Dr. Bills Receivable a/c ₹5,000; Cr. X a/c ₹5,000
(D) Dr. Cash a/c ₹4,800; Dr. Discount a/c ₹200; Cr. X a/c ₹5,000

Ans :

(D) Dr. Cash a/c ₹4,800; Dr. Discount a/c ₹200; Cr. X a/c ₹5,000
Y receives ₹4,800 in cash (Debit Cash a/c). Y also bears his share of the discount, which is an expense of ₹200 (Debit Discount a/c). The total amount of ₹5,000 represents a liability to X for the accommodation provided. Therefore, X's account is credited for ₹5,000.

Oct/Nov 2025

85. What is the primary purpose of a Bills Receivable Book?
(A) To record all bills of exchange accepted by the business.
(B) To serve as a subsidiary ledger for individual customer accounts.
(C) To track all cash received from discounting bills receivable at the bank.
(D) To record details of all bills received from customers.

Ans :

(D) To record details of all bills received from customers.
The Bills Receivable Book is a special journal or a book of original entry used to record the particulars of all the bills of exchange and promissory notes that a business receives from

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May/June 2019

106. If a drawer endorses a bill to a creditor, who becomes the 'holder' of the bill?
(A) The drawer
(B) The endorsee (the creditor)
(C) The drawee
(D) The bank

Ans :

(B) The endorsee (the creditor)
Endorsement is the legal transfer of a negotiable instrument. When the drawer endorses the bill to their creditor (the endorsee), the endorsee acquires the legal title to the bill. They become the new holder, legally entitled to receive the payment from the drawee on the due date or to further endorse it.

Oct/Nov 2012

107. In case of renewal of a bill, interest is typically:
(A) Paid by the drawer to the drawee as a fee for renewal.
(B) Paid by the drawer to the bank as a service charge.
(C) Forgone by both parties as a gesture of goodwill.
(D) Charged by the drawer to the drawee for the extended credit period.

Ans :

(D) Charged by the drawer to the drawee for the extended credit period.
Renewal of a bill is essentially an extension of credit requested by the drawee. For granting this extension, the drawer compensates for the delayed payment by charging interest on the outstanding amount for the duration of the new bill. This interest is an income for the drawer and an expense for the drawee.

May/June 2011

108. What is the nature of a 'Bills Receivable' account and a 'Bills Payable' account?
(A) Bills Receivable is an asset (real account), and Bills Payable is a liability.
(B) Both are nominal accounts.
(C) Bills Receivable is a real account, and Bills Payable is a personal account.
(D) Both are personal accounts representing debtors and creditors.

Ans :

(A) Bills Receivable is an asset (real account), and Bills Payable is a liability.
A Bill Receivable is an asset for the business, representing a right to receive money, and is classified as a real account. A Bill Payable is a liability, representing an obligation to pay money. While some older conventions classified them as personal accounts, the modern treatment sees them as assets and liabilities.

NODIA

Oct/Nov 2016

109. Which of the following NOT a valid action a drawer can take with a bill of exchange before its maturity?
(A) Retain the bill till the due date.
(B) Discount the bill with a bank.
(C) Force the drawee to pay before the due date.
(D) Endorse the bill to a creditor.

Ans :

(C) Force the drawee to pay before the due date.
The drawee's legal obligation is to pay on the maturity date, not before. While the drawee can voluntarily choose to pay early (retire the bill), the drawer cannot legally compel them to do so. The other options—retaining, discounting, and endorsing—are all standard and legitimate actions the holder of a bill can take.

May/June 2025

110. On dishonour of a bill, the holder in due course presents the bill to a notary public who records the fact of dishonour. The amount paid for this service is called 'Noting Charges'. Based on this, who initially pays the noting charges?
(A) The current holder of the bill at the time of dishonour.
(B) The drawee, who is ultimately responsible for the non-payment.
(C) The original drawer, who created the instrument.
(D) A government fund established to cover such legal costs.

Ans :

(A) The current holder of the bill at the time of dishonour.
On dishonour, the current 'holder in due course' is the one who presents the bill to the notary public. It follows that this holder is the party who engages the notary's services and is therefore responsible for the initial payment of the noting

Oct/Nov 2005

91. If a due date falls on a public holiday, when is the bill payable?
(A) On the same day.
(B) On the next working day.
(C) It is at the discretion of the drawee.
(D) On the earlier working day.

Ans :

(D) On the earlier working day.
The Negotiable Instruments Act clearly states that when the due date of a bill of exchange or promissory note falls on a public holiday, the instrument becomes payable on the preceding or earlier working day.

May/June 2021

92. A bill drawn by a creditor on a debtor for a genuine transaction is defined as a:
(A) Accommodation bill
(B) Trade bill
(C) Promissory note
(D) Cheque

Ans :

(B) Trade bill
When a creditor draws a bill on a debtor to finance an actual transaction (implying consideration like goods or services), it is referred to as a 'trade bill'. This contrasts with an accommodation bill, which lacks such a transaction.

Oct/Nov 2019

93. What is the purpose of an accommodation bill?
(A) To formally document the credit terms of a specific trade transaction.
(B) To provide security for the payment related to a purchase or sale of goods.
(C) To raise funds for parties in need, without an underlying trade transaction.
(D) To serve as an official receipt acknowledging the delivery of goods.

Ans :

(C) To raise funds for parties in need, without an underlying trade transaction.
Unlike a trade bill, which is linked to a sale, an accommodation bill's purpose is purely financial. It allows one or both parties to generate funds by discounting the bill, even when no goods have been bought or sold between them.

May/June 2024

94. On January 1, 2022, X draws a bill on Y for ₹40,000 for 3 months. What is the maturity date of the bill?
(A) April 1, 2022
(B) April 3, 2022
(C) May 4, 2022
(D) April 4, 2022

Ans :

(D) April 4, 2022
The bill is dated January 1, 2022 and has a term of 3 months. The nominal due date is April 1, 2022 (three months from January 1). To find the legal maturity date, we add three days of grace. Therefore, the maturity date is April 1, 2022 + 3 days = April 4, 2022.

NODIA

Oct/Nov 2017

95. What are noting charges?
(A) A fee paid to a notary public for certifying the dishonour of a bill.
(B) A service fee paid to the bank for processing a dishonoured instrument.
(C) A contractual penalty paid by the drawee to the drawer for non-payment.
(D) A fine paid by the holder to the drawee for presenting a bill after its due date.

Ans :

(A) A fee paid to a notary public for certifying the dishonour of a bill.
Noting charges are the fees for the official service provided by a Notary Public. This service involves formally presenting the dishonoured instrument and recording the fact of its non-payment or non-acceptance. These charges serve to create legal evidence of the dishonour and are recoverable from the party at fault.

May/June 2008

96. Which of the following statements is not true?
(A) There is no difference in appearance between a trade and accommodation bill.
(B) The Drawee is the maker of a bill of exchange.
(C) A bill of exchange must be accepted by the drawee to be valid.
(D) The creditor typically draws a bill on the debtor.

Ans :

(B) The Drawee is the maker of a bill of exchange.

The maker of a bill of exchange is the 'Drawer'. The 'Drawee' is the person on whom the bill is drawn and who is ordered to pay. The drawee becomes the 'Acceptor' after signing the bill, but they are not the maker. Therefore, the statement that the drawee is the maker of a bill is incorrect.

Oct/Nov 2007

97. Which of the following statements is true?
(A) An insolvent is a person from whom a large portion of the debt is always recoverable.
(B) The drawer can never sue the drawee in case of dishonour of an accommodation bill.
(C) When the due date of a bill falls on a public holiday, it is payable on the earlier working day.
(D) The drawee is the person to whom a bill is endorsed by the holder.

Ans :

(C) When the due date of a bill falls on a public holiday, it is payable on the earlier working day.
This statement correctly reflects the rule under the Negotiable Instruments Act. Option (A) is incorrect, as sometimes little or nothing is recoverable. Option (B) is incorrect; legal recourse may still be available. Option (D) is incorrect; the person to whom a bill is endorsed is the 'endorsee', not the 'drawee'.

May/June 2007

98. **Assertion (A) :** A bill of exchange requires acceptance by the drawee.
Reason (R) : Acceptance signifies the drawee's unconditional agreement to pay the amount of the bill on the due date.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
A bill of exchange is merely an order until the drawee accepts it. The act of acceptance transforms the drawee's moral obligation into a legally binding liability. Therefore, acceptance is necessary (A is true), and it serves as the drawee's formal promise to honour the bill (R is true and explains A).

Oct/Nov 2009

99. Identify the incorrect statement regarding a cheque.
(A) A cheque can only be drawn upon a bank.
(B) A cheque is always payable on demand.
(C) A cheque requires acceptance by the bank before payment.
(D) A cheque drawn with a future date is valid but payable only on or after that date.

Ans :

(C) A cheque requires acceptance by the bank before payment.
Unlike a bill of exchange which requires acceptance by the drawee, a cheque does not require acceptance. It is an order to the bank to pay on presentation. The bank either honours the cheque by paying it or dishonours it. The concept of formal acceptance by the bank does not apply to cheques.

May/June 2023

100. Match List-I with List-II and select the correct answer.
List-I (Term)
P. Retirement of bill
Q. Endorsement of bill
R. Noting Charges
S. Renewal of bill
List-II (Description)
1. Transfer of bill to another person
2. Cancellation of old bill and drawing a new one
3. Payment of bill before the due date
4. Fee paid to Notary Public for dishonour
(A) P-3, Q-1, R-4, S-2
(B) P-1, Q-3, R-2, S-4
(C) P-3, Q-2, R-4, S-1
(D) P-4, Q-1, R-3, S-2

Ans :

(A) P-3, Q-1, R-4, S-2
Retirement (P) is payment before the due date (3). Endorsement (Q) is transferring the bill to another person (1). Noting Charges (R) are fees paid to a Notary Public for recording dishonour (4). Renewal (S) involves cancelling the old bill and drawing a new one (2). The correct matching is P-3, Q-1, R-4, S-2.

Oct/Nov 2022

101. Consider the following statements regarding a 'Holder in due course':

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1. He must have obtained the instrument for valuable consideration.
2. He must have become the holder after the instrument's maturity.
3. He must not have any reason to believe there was a defect in the previous holder's title.

Which of the above statements is/are correct?
(A) 1 only
(B) 1 and 2 only
(C) 1 and 3 only
(D) 1, 2 and 3

Ans :

(C) 1 and 3 only
The status of 'Holder in due course' requires three conditions to be met. The holder must acquire the instrument for value and in good faith (without notice of title defects). Crucially, this acquisition must happen before the instrument's maturity date. Statement 2 is incorrect as it states the opposite, invalidating that condition.

May/June 2016

102. A sells goods to B for ₹25,000 and draws a bill for 2 months. B accepts the bill. In B's books, this bill is considered:
(A) A Bill Payable and a liability.
(B) A Bill Receivable and an asset.
(C) A Trade Receivable and an asset.
(D) A Promissory Note and a liability.

Ans :

(A) A Bill Payable and a liability.
For the person who has to pay against a bill (the drawee/acceptor), the instrument represents a formal obligation to pay a certain sum on a future date. In accounting, this obligation is classified as a liability under the account head 'Bills Payable'. It is a formal acknowledgment of debt owed to the drawer.

Oct/Nov 2014

103. Which of the following pairs is incorrectly matched?
(A) Drawer : Person who draws the bill
(B) Drawee : Person on whom the bill is drawn
(C) Payee : Person who makes the promise in a promissory note
(D) Maker : Person who makes a promissory note

Ans :

(C) Payee : Person who makes the promise in a promissory note
The 'Payee' is the person who is entitled to receive the money under either a bill of exchange or a promissory note. The person who makes the promise in a promissory note is called the 'Maker'. Therefore, the pairing of Payee with the description of the Maker is incorrect.

May/June 2010

104. Statement I: For accounting purposes, no distinction is made between bills of exchange and promissory notes.
Statement II : Both bills of exchange and promissory notes create a legally enforceable right to receive or an obligation to pay a sum of money.
(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Statement I is correct, but Statement II is incorrect.
(D) Statement I is incorrect, but Statement II is correct.

Ans :

(A) Both Statement I and Statement II are correct.
Statement I is correct; in the books of accounts, both instruments are recorded as either 'Bills Receivable' or 'Bills Payable'. Statement II provides the correct reason for this practice: both instruments serve the same fundamental financial purpose of creating a formal, legally recognized debt, making their accounting treatment identical.

Oct/Nov 2006

105. A bill drawn on May 15 for 30 days will have a maturity date of:
(A) June 14
(B) June 15
(C) June 17
(D) June 16

Ans :

(C) June 17
To calculate the due date, we count 30 days from May 15. May has 31 days, so there are 16 days left in May (31-15). We need 14 more days in June to complete 30 days. So the nominal due date is June 14. Adding three days of grace (14 + 3), the maturity date becomes June 17.

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Ans :

(A) The drawer records liability to the bank, makes the drawee liable, charges interest, and draws a new bill.
The entries show several sequential steps. First, the drawer records the payment to the bank for the dishonoured bill and noting charges. Second, he makes the drawee liable for this amount. Third, he charges interest to the drawee. Finally, he draws a new bill covering the entire balance due.

May/June 2008

66. What is the journal entry in the drawer's books when a new bill for ₹16,540 is duly met on maturity?
(A) Dr. Cash/Bank a/c ₹16,540; Cr. Chetan a/c ₹16,540
(B) Dr. Cash/Bank a/c ₹16,540; Cr. Bills Receivable a/c ₹16,540
(C) Dr. Bills Receivable a/c ₹16,540; Cr. Cash/Bank a/c ₹16,540
(D) Dr. Chetan a/c ₹16,540; Cr. Bills Receivable a/c ₹16,540

Ans :

(B) Dr. Cash/Bank a/c ₹16,540; Cr. Bills Receivable a/c ₹16,540
When the bill is honoured, the drawer receives the payment. This increases his cash or bank balance, so the Cash/Bank account is debited for ₹16,540. The asset represented by 'Bills Receivable' is now realized, so the account is credited to remove it from the books.

Oct/Nov 2007

67. Sheetal holds a bill from Deepal for ₹5,000, which she endorses to Tinku. The bill is dishonoured, and noting charges are ₹100. What entry does Sheetal pass to record her liability to Tinku?
(A) Dr. Deepal a/c ₹5,100; Cr. Tinku a/c ₹5,100
(B) Dr. Tinku a/c ₹5,100; Cr. Deepal a/c ₹5,100
(C) Dr. Deepal a/c ₹5,100; Cr. Bills Receivable a/c ₹5,000; Cr. Noting Charges a/c ₹100
(D) Dr. Bills Receivable a/c ₹5,000; Dr. Noting charges a/c ₹100; Cr. Tinku a/c ₹5,100

Ans :

(D) Dr. Bills Receivable a/c ₹5,000; Dr. Noting charges a/c ₹100; Cr. Tinku a/c ₹5,100
Upon dishonour of the endorsed bill, Sheetal becomes liable to Tinku for the bill amount plus noting charges. Her liability to Tinku increases, so Tinku's account is credited for ₹5,100. Sheetal gets the bill back, so Bills Receivable is debited (₹5,000), and the noting charges paid by Tinku are also debited.

May/June 2007

68. Following the dishonour of an endorsed bill, the original drawer (Sheetal) makes the original drawee (Deepal) liable for the total amount. What is the journal entry for this in Sheetal's books?
(A) Dr. Deepal a/c ₹5,100; Cr. Bills Receivable a/c ₹5,000; Cr. Noting Charges a/c ₹100
(B) Dr. Deepal a/c ₹5,100; Cr. Tinku a/c ₹5,100
(C) Dr. Bills Receivable a/c ₹5,100; Cr. Deepal a/c ₹5,100
(D) Dr. Tinku a/c ₹5,100; Cr. Bills Receivable a/c ₹5,100

Ans :

(A) Dr. Deepal a/c ₹5,100; Cr. Bills Receivable a/c ₹5,000; Cr. Noting Charges a/c ₹100
After becoming liable to Tinku, Sheetal passes this liability on to Deepal, the original acceptor. Deepal's account is debited for the total amount of ₹5,100, making him a debtor again. The Bills Receivable and Noting Charges accounts, which were debited in the previous step, are now credited to transfer the amounts to Deepal's account.

Oct/Nov 2009

69. After a dishonour, Deepal owes Sheetal ₹5,100. Deepal pays ₹2,000 cash and accepts a new bill for the balance plus ₹200 interest. What is the amount of the new bill?
(A) ₹3,100
(B) ₹5,100
(C) ₹3,300
(D) ₹2,200

Ans :

(C) ₹3,300
The total amount receivable from Deepal was ₹5,100. He paid ₹2,000 in cash, leaving a balance of ₹3,100. An additional interest of ₹200 is charged. Therefore, the amount of the new bill is the balance plus interest, which is ₹3,100 + ₹200 = ₹3,300.

May/June 2023

70. A new bill for ₹3,300 is dishonoured, and the holder pays ₹200 for noting charges. What is the total amount now due from the drawee?

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charges. These charges are later recovered from the party at fault (the drawee).

Oct/Nov 2010

111. For a bill of exchange, 'Notice of dishonour is necessary,' but for a cheque, 'Notice of dishonour is not necessary.' What can be inferred from this distinction?

(A) The drawer of a dishonoured cheque is not liable for payment.
(B) Banks are not required to inform customers about a dishonoured cheque.
(C) Dishonour of a cheque has no legal consequences.
(D) To hold the drawer of a bill of exchange liable, the holder must give them a notice of dishonour.

Ans :

(D) To hold the drawer of a bill of exchange liable, the holder must give them a notice of dishonour. The necessity of a 'notice of dishonour' for a bill of exchange is a legal requirement. If the acceptor dishonours the bill, the holder must inform the drawer and any prior endorsers. Failure to give this notice can discharge these parties from their liability. For a cheque, this formal notice is not required to hold the drawer liable.

May/June 2005

112. A bill is drawn for "Two months after date". If the date of the bill is March 10, 2022, what is its legal due date?

(A) May 10, 2022
(B) May 13, 2022
(C) May 12, 2022
(D) June 10, 2022

Ans :

(B) May 13, 2022
The term is two months from the date of the bill. Two months from March 10, 2022, is May 10, 2022. To this nominal due date, three days of grace must be added. Therefore, the legal due date for payment is May 10 + 3 days = May 13, 2022.

Oct/Nov 2014

113. Identify the correct chronological order of events for a bill that is renewed.

1. Cancellation of the old bill.
2. Request for renewal by the drawee.
3. Drawing and acceptance of a new bill.
4. Charging of interest by the drawer.

(A) 2, 1, 4, 3
(B) 1, 2, 3, 4
(C) 2, 4, 1, 3
(D) 4, 2, 1, 3

Ans :

(A) 2, 1, 4, 3
The process begins with the drawee's request for renewal (2). Following this, the drawer agrees and the first accounting step is to cancel the old bill (1). The drawer then calculates and charges interest for the new term (4). Finally, a new bill is drawn for the balance plus interest and is accepted by the drawee (3).

May/June 2012

114. Which of the following statements is correct?

1. Bills Receivable is an asset for the drawer.
2. Bills Payable is a liability for the drawee.
3. In an accommodation bill, there is no underlying trade consideration.

(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(D) 1, 2, and 3
All three statements are correct. A Bill Receivable represents a right to receive money, making it an asset for the drawer. A Bill Payable represents an obligation to pay, making it a liability for the drawee. An accommodation bill is distinguished from a trade bill precisely because it lacks an underlying sale or purchase consideration.

Oct/Nov 2025

115. Which of the following statements regarding a promissory note is incorrect?

(A) It requires acceptance by the payee to be valid.
(B) It contains an unconditional undertaking to pay.
(C) It is made by the debtor.
(D) It involves two parties: the maker and the payee.

Ans :

(A) It requires acceptance by the payee to be valid.
A promissory note is a promise made by the maker (debtor) to the payee (creditor). It does not require 'acceptance' because it is not an order. The

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maker is already the party promising to pay, so there is no need for a separate act of acceptance. The instrument is valid once properly made and signed by the maker.

May/June 2020

116. Ramesh renews a bill for Suresh. The balance due is ₹6,000 and interest charged is ₹150. What is the journal entry in Ramesh's (drawer's) books for receiving a part payment of ₹4,000 and a new bill?

(A) Dr. Cash a/c ₹4,000; Dr. Bills Receivable a/c ₹6,150; Cr. Suresh a/c ₹10,000; Cr. Interest a/c ₹150

(B) Dr. Cash a/c ₹4,000; Dr. Bills Receivable a/c ₹6,150; Cr. Suresh a/c ₹10,150

(C) Dr. Cash a/c ₹4,000; Dr. Bills Receivable a/c ₹6,000; Dr. Interest a/c ₹150; Cr. Suresh a/c ₹10,150

(D) Dr. Cash a/c ₹4,000; Dr. Bills Receivable a/c ₹6,150; Cr. Interest a/c ₹150; Cr. Suresh a/c ₹10,000

Ans :

(D) Dr. Cash a/c ₹4,000; Dr. Bills Receivable a/c ₹6,150; Cr. Interest a/c ₹150; Cr. Suresh a/c ₹10,000

The entry reflects all parts of the renewal settlement. Ramesh receives cash (Dr. Cash ₹4,000) and a new bill (Dr. Bills Receivable ₹6,150). The interest of ₹150 is his income (Cr. Interest). These receipts settle the total amount owed by Suresh, which was the original ₹10,000 (Cr. Suresh's account which was debited during cancellation).

Oct/Nov 2013

117. Sheetal is owed ₹3,500 by Deepal, who becomes bankrupt. Sheetal receives a final dividend of 50 % from Deepal's estate. What is the journal entry passed by Sheetal?

(A) Dr. Cash a/c ₹3,500; Cr. Deepal a/c ₹3,500

(B) Dr. Cash a/c ₹1,750; Dr. Bad Debts a/c ₹1,750; Cr. Deepal a/c ₹3,500

(C) Dr. Cash a/c ₹1,750; Cr. Deepal a/c ₹1,750

(D) Dr. Deepal a/c ₹3,500; Cr. Cash a/c ₹1,750; Cr. Bad Debts a/c ₹1,750

Ans :

(B) Dr. Cash a/c ₹1,750; Dr. Bad Debts a/c ₹1,750; Cr. Deepal a/c ₹3,500

The entry closes Deepal's account. The total due from Deepal was ₹3,500, so her account is credited for the full amount. Sheetal receives 50 % in cash (Dr. Cash a/c ₹1,750). The remaining unrecoverable 50% is an expense, so it is debited to the Bad Debts account (Dr. Bad Debts a/c ₹1,750).

May/June 2015

118. Deepal owes Sheetal ₹3,500 and becomes bankrupt. Her estate makes a final payment of 50 % of the amount due. What entry reflects this transaction in Deepal's books?

(A) Dr. Sheetal a/c ₹3,500; Cr. Cash a/c ₹1,750; Cr. Deficiency a/c ₹1,750

(B) Dr. Sheetal a/c ₹3,500; Cr. Cash a/c ₹3,500

(C) Dr. Sheetal a/c ₹3,500; Cr. Deficiency a/c ₹3,500

(D) Dr. Cash a/c ₹1,750; Dr. Deficiency a/c ₹1,750; Cr. Sheetal a/c ₹3,500

Ans :

(A) Dr. Sheetal a/c ₹3,500; Cr. Cash a/c ₹1,750; Cr. Deficiency a/c ₹1,750

This entry settles the liability towards Sheetal. Deepal's liability to Sheetal is debited to close the account (Dr. Sheetal a/c ₹3,500). The actual cash paid out is credited (Cr. Cash a/c ₹1,750). The unpaid balance, representing the shortfall due to insolvency, is transferred to the Deficiency account (Cr. Deficiency a/c ₹1,750).

Oct/Nov 2020

119. X remits 50% of the proceeds of a discounted accommodation bill to Y. The face value was ₹10,000, and proceeds were ₹9,600. What is the entry in X's books to record the remittance to Y?

(A) Dr. Y's a/c ₹5,000; Cr. Cash a/c ₹5,000

(B) Dr. Y's a/c ₹4,800; Cr. Cash a/c ₹4,800

(C) Dr. Y's a/c ₹5,000; Cr. Bills Receivable a/c ₹5,000

(D) Dr. Y's a/c ₹5,000; Cr. Cash a/c ₹4,800; Cr. Discount a/c ₹200

Ans :

(D) Dr. Y's a/c ₹5,000; Cr. Cash a/c ₹4,800; Cr. Discount a/c ₹200

X debits Y for half the face value of the bill (₹5,000), as this is the extent of accommodation Y has received. X credits Cash for the amount actually sent (₹4,800, which is half of ₹9,600). The difference of ₹200 is credited to Discount, effectively transferring half of the discount expense to Y.

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May/June 2018

120. What is the purpose of the "How Disposed off" column in a Bills Receivable Book?

(A) To track the final disposition of the bill (e.g., honoured, discounted).

(B) To record the full legal name and address of the drawee.

(C) To calculate and record the legal maturity date of the bill.

(D) To record the face value of the bill in both numbers and words.

Ans :

(A) To track the final disposition of the bill (e.g., honoured, discounted).

The "How Disposed off" column is a memorandum column used for tracking the status and final outcome of each bill receivable. It helps the accountant to know whether a particular bill was paid on maturity (honoured), sold to the bank (discounted), transferred to a creditor (endorsed), or dishonoured, providing a quick reference for its status.

Oct/Nov 2005

121. A draws a bill on B. A sends this bill to his bank for collection. On the due date, B honours the bill. What two entries will be passed in A's books to record sending the bill for collection and its subsequent honour?

(A) 1. Dr. Bank for Bill Collection, Cr. B's a/c; 2. Dr. Cash, Cr. Bank for Bill Collection

(B) 1. Dr. Bank a/c, Cr. Bills Receivable; 2. No entry required.

(C) 1. Dr. Bank for Bill Collection, Cr. Bills Receivable; 2. Dr. Cash, Cr. Bank for Bill Collection

(D) 1. Dr. B's a/c, Cr. Bills Receivable; 2. Dr. Cash, Cr. B's a/c

Ans :

(C) 1. Dr. Bank for Bill Collection, Cr. Bills Receivable; 2. Dr. Cash, Cr. Bank for Bill Collection

First, when the bill is sent for collection, it is transferred from the 'Bills Receivable' account to a temporary holding account, 'Bank for Bill Collection' (Entry 1). Second, when the bank collects the cash and remits it, the cash account is debited, and the temporary 'Bank for Bill Collection' account is credited to close it (Entry 2).

May/June 2021

122. A bill for ₹10,000 sent to the bank for collection by A is dishonoured. The bank pays ₹100 noting charges. What entry will A pass to make B (the drawee) liable for the total amount due?

(A) Dr. B's a/c ₹10,100; Cr. Bill Receivable a/c ₹10,000; Cr. Noting Charges a/c ₹100

(B) Dr. B's a/c ₹10,100; Cr. Bank a/c ₹10,100

(C) Dr. B's a/c ₹10,000; Dr. Noting Charges a/c ₹100; Cr. Bank for Bill Collection a/c ₹10,100

(D) Dr. B's a/c ₹10,100; Cr. Bank for Bill Collection a/c ₹10,000; Cr. Cash a/c ₹100

Ans :

(D) Dr. B's a/c ₹10,100; Cr. Bank for Bill Collection a/c ₹10,000; Cr. Cash a/c ₹100

Upon dishonour, B is made a debtor again for the total amount owed (Dr. B's a/c ₹10,100). The temporary account 'Bank for Bill Collection' is credited to reverse the entry made when the bill was sent for collection. The cash paid by A for noting charges is also credited (Cr. Cash a/c ₹100).

Oct/Nov 2019

123. Suresh requests Ramesh to renew a ₹10,000 bill. Suresh pays ₹4,000 in cash and accepts a new bill for the balance plus ₹150 interest. What is the compound journal entry for this entire transaction in Suresh's (the drawee's) books?

(A) Dr. Ramesh a/c ₹10,000; Dr. Interest a/c ₹150; Cr. Cash a/c ₹4,150; Cr. Bills Payable a/c ₹6,000

(B) Dr. Ramesh a/c ₹10,150; Cr. Cash a/c ₹4,000; Cr. Bills Payable a/c ₹6,150

(C) Dr. Bills Payable a/c ₹10,000; Dr. Interest a/c ₹150; Cr. Cash a/c ₹4,000; Cr. Ramesh a/c ₹6,150

(D) Dr. Ramesh a/c ₹10,000; Dr. Interest a/c ₹150; Cr. Cash a/c ₹4,000; Cr. Bills Payable a/c ₹6,150

Ans :

(D) Dr. Ramesh a/c ₹10,000; Dr. Interest a/c ₹150; Cr. Cash a/c ₹4,000; Cr. Bills Payable a/c ₹6,150

This single compound entry reflects the entire renewal process in the drawee's books. It settles the liability to Ramesh arising from the cancellation of the old bill (Dr. ₹10,000), recognizes the interest expense (Dr. ₹150), records the partial cash payment (Cr. ₹4,000), and creates the new liability for the new bill (Cr. Bills Payable ₹6,150).

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CHAPTER 9

Operational Aspects of Accounting Entries

Oct/Nov 2012

1. What is the ultimate objective of recording financial transactions in any business enterprise?

(A) To calculate daily cash balances for managing immediate operational funding requirements.

(B) To prepare the balance sheet and P&L account for reporting on financial position and performance.

(C) To facilitate internal and external audits by providing a complete transaction trail for verification.

(D) To maintain debit and credit records for ensuring compliance with statutory reporting obligations.

Ans :

(B) To prepare the balance sheet and P&L account for reporting on financial position and performance.

The primary goal of recording financial transactions is to compile the balance sheet and the Profit & Loss account. These statements offer stakeholders a transparent view of the enterprise's operational results during an accounting period and its financial standing at the end of that period, which is crucial for decision-making and assessment of performance.

May/June 2021

2. According to the principles of modern accounting, which system is used that implies no standalone entry can exist in the books?

(A) Double Entry System

(B) Single Entry System

(C) Cash Basis System

(D) Accrual Basis System

Ans :

(A) Double Entry System

Modern accounting is based on the double-entry system. This fundamental principle dictates that every financial transaction has two aspects, a debit and a credit. Consequently, there can be no standalone entry; every debit entry must have a corresponding credit entry, ensuring that the accounting equation always remains in balance after each transaction.

Oct/Nov 2005

3. If a customer deposits cash of ₹2,000 into their bank account, what is the correct pair of accounting entries?

(A) Debit customer account by ₹2,000 and Credit cash account by ₹2,000.

(B) Debit suspense account by ₹2,000 and Credit cash account by ₹2,000.

(C) Credit customer account by ₹2,000 and Debit cash account by ₹2,000.

(D) Credit interest account by ₹2,000 and Debit customer account by ₹2,000.

Ans :

(C) Credit customer account by ₹2,000 and Debit cash account by ₹2,000.

When a customer deposits cash, the bank's cash holding (an asset) increases, which is recorded as a debit to the cash account. Simultaneously, the bank's liability to the customer increases, which is recorded as a credit to the customer's account. This follows the double-entry principle, reflecting the increase in assets and corresponding liabilities.

May/June 2008

4. What is a peculiar feature of the accounting entry process in a bank's manual operations compared to other enterprises?

(A) Entries are first made in the journal (day book) and then posted to ledgers.

(B) Entries are only made in the General Ledger, bypassing subsidiary ledgers.

(C) Entries are directly posted to the P&L account without affecting ledgers.

(D) Entries are first made in the ledger accounts and then in the journal (day book).

Ans :

(D) Entries are first made in the ledger accounts and then in the journal (day book).

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(A) The notary public, as part of their official duties.
(B) The bank that discounted the bill, as a service fee.
(C) Any prior party liable on the bill.
(D) Only the original drawer of the bill.

Ans :

(C) Any prior party liable on the bill.
The holder who pays the noting charges has the right to recover them from any party liable on the bill. This includes the acceptor (drawee) who was primarily responsible for payment, as well as the drawer and any previous endorsers, who are secondarily liable for the full amount including these charges.

May/June 2023

130. Consider the following statements:
1. A promissory note contains an unconditional order to pay.
2. A bill of exchange is drawn by a creditor on a debtor.
3. A cheque does not require stamping.
4. A bill of exchange is always payable on demand.

Which of the above statements are correct?
(A) 1 and 4
(B) 2 and 3
(C) 1, 2, and 3
(D) 2, 3, and 4

Ans :

(B) 2 and 3
Statement 1 is incorrect; a promissory note contains an unconditional 'undertaking'. Statement 4 is incorrect; a bill of exchange can be payable after a certain period (a time bill). Statements 2 and 3 are correct. A bill of exchange is typically drawn by a creditor, and a cheque does not require a stamp.

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While some vouchers evidence only a debit or only a credit, a 'composite voucher' is one that contains particulars for both debit and credit components of a transaction affecting different accounts. This type of voucher is convenient for recording transactions that have multiple effects, such as error rectifications or internal fund movements, in a single document.

May/June 2012

18. Which of the following is classified as a debit voucher in banking operations?
(A) Cheques issued by the customers.
(B) Pay-in-slips filled by customers for depositing amounts.
(C) Applications for issue of term deposits.
(D) Challans for deposits into government accounts.

Ans :

(A) Cheques issued by the customers.
A cheque issued by a customer is an instruction to the bank to pay a certain sum of money from their account. When the bank honors this cheque, it debits the customer's account to reduce the balance. Therefore, a customer's cheque serves as a primary type of debit voucher for the bank.

Oct/Nov 2007

19. A withdrawal form received from a savings bank account holder serves as what type of voucher for the bank?
(A) A credit voucher
(B) A composite voucher
(C) A debit voucher
(D) A transfer voucher

Ans :

(C) A debit voucher
A withdrawal form is a document used by a savings bank account holder to take cash out of their account. For the bank, this transaction results in a reduction of its liability to the customer. This reduction is recorded as a debit to the customer's savings account, making the withdrawal form a debit voucher.

May/June 2019

20. When a draft issued by another branch is presented for payment at your branch, it acts as which type of voucher?
(A) Credit voucher
(B) Internal voucher
(C) Contra voucher
(D) Debit voucher

Ans :

(D) Debit voucher
A draft is a pre-paid instrument. When a draft issued by another branch is paid at your branch, your branch makes the payment on behalf of the issuing branch. The amount is debited to an inter-office account or the Drafts Payable account. Thus, the presented draft itself functions as a debit voucher for the paying branch.

Oct/Nov 2024

21. Which of the following is NOT a debit voucher?
(A) Dividend warrants issued by a bank's corporate customer that are made payable at the branch.
(B) Travellers' cheques issued by any branch of the bank when they are presented for encashment.
(C) A pay-in-slip that is properly filled out for a cash deposit into a savings account.
(D) A letter of authority from a customer containing standing instructions for a periodic account debit.

Ans :

(C) A pay-in-slip that is properly filled out for a cash deposit into a savings account.
A pay-in-slip is used to deposit funds into an account. This action increases the bank's liability to the customer, requiring a credit to the customer's account. Therefore, a pay-in-slip is a credit voucher. The other options listed are all instruments or instructions that result in a debit to an account.

May/June 2024

22. If a draft issued by a branch is cancelled at the customer's request and the amount is refunded, the cancelled draft instrument serves as a:
(A) Credit voucher for the refund amount.
(B) Debit voucher for the refund amount.
(C) Composite voucher for the cancellation.
(D) Non-accounting instrument with no voucher status.

Ans :

(B) Debit voucher for the refund amount.
When a draft is initially issued, the bank receives money and credits a liability account (like Drafts Payable). If this draft is cancelled, the bank

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A unique aspect of bank accounting, especially in manual systems, is that entries are first posted directly to the concerned ledger accounts. Only after this are all entries for a ledger head summarized in the journal or day book. This contrasts with typical businesses where entries are first recorded in a journal before ledger posting.

Oct/Nov 2023

5. In a manual banking environment, what is the mandatory basis for making any accounting entry?

(A) A verbal instruction from a regular customer, confirmed via a recorded phone call.

(B) An email confirmation from the branch manager, which is digitally signed for authenticity.

(C) A physical voucher that is properly filled out and authenticated by an authorised officer.

(D) A provisional entry logged in a temporary system memo pad, pending end-of-day verification.

Ans :

(C) A physical voucher that is properly filled out and authenticated by an authorised officer.

In manual banking operations, no accounting entry can be made without a corresponding physical voucher. This voucher serves as the primary evidence of the transaction and must be properly authenticated by a designated officer of the branch. This ensures control, auditability, and authorization for every single transaction processed by the bank's staff.

May/June 2013

6. In a computerized banking environment, after a staff member makes an entry, what is the subsequent crucial step?

(A) The system automatically generates and prints a physical copy of the voucher for archival filing.

(B) The entry is digitally authenticated by a designated official directly within the banking system.

(C) The customer is immediately notified via an automated phone call or SMS for transaction confirmation.

(D) The entry is manually transcribed from the system's screen into the physical General Ledger book.

Ans :

(B) The entry is digitally authenticated by a designated official directly within the banking system.

In computerized banking, after a staff member inputs a transaction, it requires authentication by an authorized official within the system. This digital authorization replaces the physical signature on a manual voucher. Once authenticated, the system automatically handles the subsequent processes like updating day books and the General Ledger, ensuring a secure and streamlined workflow.

Oct/Nov 2016

7. Why is it still important for bank staff to understand the manual system of accounting even in a computerized environment?

(A) Because computer systems are inherently unreliable and are prone to frequent, unrecoverable data failures.

(B) To gain the ability to manually override system-generated financial statements if they appear to be incorrect.

(C) To be able to perform dual roles in both manual and computerized branches simultaneously if required by staffing needs.

(D) To understand the underlying process and thereby capably answer queries from customers and auditors.

Ans :

(D) To understand the underlying process and thereby capably answer queries from customers and auditors.

Even with widespread computerization, understanding the manual accounting process is vital for bank staff. This knowledge provides clarity on the fundamental workflow behind the automated system. It enables them to confidently and accurately respond to inquiries from customers and auditors regarding how transactions are processed, rather than claiming ignorance of the underlying procedures.

May/June 2018

8. What is the primary reason for the stronger need for accuracy and up-to-date ledger accounts in banks compared to other enterprises?

(A) To effectively manage customer accounts and maintain the essential trust placed in the institution.

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May/June 2024

124. A bill for ₹14,000 was endorsed by Bimal to Tarun. On the due date, the bill is honoured. What entry, if any, is passed in Bimal's books upon the honour of this bill?
(A) Dr. Cash a/c ₹14,000; Cr. Bills Receivable No. 1 a/c ₹14,000
(B) Dr. Tarun a/c ₹14,000; Cr. Chetan a/c ₹14,000
(C) Dr. Chetan a/c ₹14,000; Cr. Bills Receivable No. 1 a/c ₹14,000
(D) No entry is passed.

Ans :

(D) No entry is passed.
When Bimal endorsed the bill to Tarun, he transferred his rights. Upon the bill's honour, the drawee pays the endorsee (Tarun) directly. Since Bimal is no longer part of this specific transaction, no entry is required in his books. His contingent liability is simply extinguished without an accounting entry.

Oct/Nov 2017

125. A bill of ₹5,000 was discounted by Sheetal for ₹4,950. The bill was met in due course. What entry did Sheetal pass when the bill was met?
(A) No entry is passed.
(B) Dr. Cash a/c ₹5,000; Cr. Bills Receivable No. 2 a/c ₹5,000
(C) Dr. Deepal a/c ₹5,000; Cr. Bank a/c ₹5,000
(D) Dr. Bank a/c ₹50; Cr. Discount a/c ₹50

Ans :

(A) No entry is passed.
Sheetal had already received her money (₹4,950) when she discounted the bill. On the due date, the drawee pays the full ₹5,000 directly to the bank. This transaction is between the drawee and the bank. Since Sheetal is not involved in this final payment, no entry is required in her books. Her contingent liability ceases.

May/June 2008

126. In an accommodation bill scenario, X draws on Y for ₹10,000 and Y draws on X for ₹9,000. These are known as:
(A) Trade Bills
(B) Renewal Bills
(C) Inland Bills
(D) Cross Bills

Ans :

(D) Cross Bills
When two parties draw bills on each other for mutual accommodation, these bills are referred to as 'Cross Bills'. The purpose is for each party to use the bill they receive to raise funds by discounting it. This is a common method for arranging reciprocal financial accommodation without any actual trade.

Oct/Nov 2007

127. Statement I: In an accommodation bill, there is no debtor-creditor relationship arising from a trade transaction.
Statement II : The purpose of an accommodation bill is to provide financial help to one or both parties.
(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Statement I is correct, but Statement II is incorrect.
(D) Statement I is incorrect, but Statement II is correct.

Ans :

(A) Both Statement I and Statement II are correct.
Both statements accurately describe the nature of an accommodation bill. Statement I is correct because these bills are not based on a sale or loan, hence no prior trade debt exists. Statement II correctly identifies their purpose, which is to create a negotiable instrument that can be discounted to raise funds for financial needs.

May/June 2007

128. A bill is drawn on January 30th for one month. What is its maturity date?
(A) March 3rd (or March 2nd in a leap year)
(B) February 28th (or 29th in a leap year)
(C) March 1st
(D) March 2nd

Ans :

(A) March 3rd (or March 2nd in a leap year)
A bill drawn for a term of one month from January 30th would nominally mature on the last day of February (February 28th in a non-leap year or February 29th in a leap year). Adding three days of grace gives a final maturity date of March 3rd (in a non-leap year) or March 2nd (in a leap year).

Oct/Nov 2009

129. If a bill is dishonoured, the holder can recover the noting charges from:

NODIA

maintaining the integrity of the bank's financial records.

Oct/Nov 2019

13. Which of the following best describes a 'transfer transaction' in a bank?
(A) A transaction that involves only the physical movement of cash, either as a deposit or a withdrawal.
(B) A transaction that is physically transferred to another branch location for its final processing and settlement.
(C) A non-cash transaction where funds are moved between customer accounts or internal bank accounts.
(D) A transaction that is cancelled by the customer and subsequently reversed by the bank on the same day.

Ans :

(C) A non-cash transaction where funds are moved between customer accounts or internal bank accounts.
A 'transfer transaction' is another term for a non-cash transaction. In such cases, funds are moved between accounts without the involvement of physical cash. These transactions can affect two customer accounts, or one customer account and one internal bank account, such as a draft account or an interest account, facilitating inter-account adjustments.

May/June 2015

14. If customer 'A' deposits a cheque drawn by customer 'B', both being customers of the same branch, which accounts are affected?
(A) The accounts of customer 'A' and the bank's cash account.
(B) The account of customer 'A' and the bank's suspense account.
(C) The account of customer 'B' and the bank's profit and loss account.
(D) The accounts of customer 'A' and customer 'B'.

Ans :

(D) The accounts of customer 'A' and customer 'B'.
When a customer deposits a cheque drawn on another customer of the same branch, it is a transfer transaction. The account of the depositor, customer 'A', is credited, and the account of the cheque issuer, customer 'B', is debited. This transaction involves a direct transfer of funds between two customer accounts within the branch.

Oct/Nov 2014

15. When a bank pays interest on deposit accounts, which internal account of the branch is typically debited?
(A) The 'Interest Account'.
(B) The 'Drafts Payable' account.
(C) The 'Suspense' account.
(D) The 'Cash' account.

Ans :

(A) The 'Interest Account'.
The payment of interest on deposits is an expense for the bank. To record this, the 'Interest Account', which is an internal expense account of the branch, is debited. Concurrently, the individual deposit accounts of the various customers are credited with their respective interest amounts, reflecting the bank's increased liability to them.

May/June 2006

16. What is the general term for the instruments used to evidence both debit and credit operations on all accounts in a bank?
(A) Ledgers
(B) Vouchers
(C) Journals
(D) Advices

Ans :

(B) Vouchers
All debit and credit transactions in a bank, whether initiated by customers or the bank itself, are executed and evidenced by means of vouchers. These documents provide the necessary details and authorization for each transaction, serving as the source document for posting entries into the respective accounts, thereby forming the foundation of the audit trail.

Oct/Nov 2021

17. A voucher that contains details for both a debit and a credit to different accounts is known as a:
(A) Simple voucher
(B) Composite voucher
(C) Debit voucher
(D) Credit voucher

Ans :

(B) Composite voucher

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(B) To strictly comply with international accounting standards, which are more stringent for financial institutions.
(C) To facilitate the faster and more accurate calculation of various complex service charges and fees.
(D) To simplify the otherwise complex and time-consuming process of preparing the annual financial report.

Ans :

(A) To effectively manage customer accounts and maintain the essential trust placed in the institution.
In banking, the necessity for ledger accounts, especially customer accounts, to be precise and current is paramount. A bank cannot afford inaccuracies as it directly impacts customer funds and trust. Every transaction must be entered immediately to reflect the correct financial position of the customer, which is a more critical and immediate requirement than in many other industries.

Oct/Nov 2011

9. In the context of banking, which books of prime entry receive relatively lesser emphasis compared to ledgers?
(A) Subsidiary ledgers and control accounts.
(B) Purchase day book and sales day book.
(C) Cash books and journals.
(D) General Ledger.

Ans :

(C) Cash books and journals.
Unlike most enterprises where books of prime entry like cash books and journals are the first point of record, banks place less emphasis on them initially. Instead, banks prioritize posting transactions directly to subsidiary ledgers. The journals or day books are compiled later from these ledger entries, highlighting a procedural difference in banking accounting.

May/June 2025

10. What is the accounting procedure followed by banks where vouchers are posted directly to individual accounts in subsidiary ledgers?
(A) Voucher Posting
(B) Journal Posting
(C) General Ledger Posting
(D) Daily Posting

Ans :

(A) Voucher Posting
Banks adhere to an accounting procedure known as 'voucher posting'. Under this system, transaction vouchers are not first entered into a journal. Instead, they are posted straightaway into the respective individual accounts within the subsidiary ledgers, such as savings, current, or loan accounts, ensuring immediate updating of customer-level records.

Oct/Nov 2008

11. Under the 'voucher posting' system, how is the respective control account in the general ledger updated?
(A) Each voucher is individually posted to the control account after subsidiary posting.
(B) The opening balance of the subsidiary ledger is posted to the control account daily.
(C) An estimate is posted daily and adjusted at the end of the month based on reconciliation.
(D) The total from separate voucher summary sheets is posted to the control account.

Ans :

(D) The total from separate voucher summary sheets is posted to the control account.
In the voucher posting method, after individual postings to subsidiary ledgers, all debit and credit vouchers for a specific transaction type are aggregated on voucher summary sheets. It is the total from these summary sheets that is then posted to the corresponding control account (e.g., Savings Bank Control Account) in the general ledger.

May/June 2010

12. How frequently is the general ledger trial balance typically prepared in a bank?
(A) Weekly
(B) Every day
(C) Monthly
(D) Annually

Ans :

(B) Every day
A key control and reconciliation feature in banking operations is the preparation of the general ledger trial balance. To ensure the books are balanced and to detect errors promptly, this trial balance is prepared at the end of each business day. This daily routine is critical for

NODIA

has to reverse the entry and refund the money. The cancelled draft instrument authorizes this reversal, which involves debiting the Drafts Payable account to extinguish the liability.

Oct/Nov 2010

23. A debit advice received from another branch for the realization of a collection instrument sent by your branch acts as a:
(A) Credit voucher
(B) Memo voucher
(C) Suspense voucher
(D) Debit voucher

Ans :

(D) Debit voucher
When your branch sends an instrument for collection to another branch, and that branch collects the payment, it will send a debit advice to your branch. This advice signifies that the other branch has debited your branch's account in its books. Your branch will use this advice as a debit voucher to debit the inter-office account.

May/June 2005

24. A term deposit receipt presented for payment at maturity is an example of what kind of voucher?
(A) A debit voucher
(B) A credit voucher
(C) A composite voucher
(D) A contingent voucher

Ans :

(A) A debit voucher
A term deposit receipt represents a liability of the bank. When this receipt is presented for payment, renewal, or premature closure, the bank must pay out the funds, thereby extinguishing or altering this liability. The operation involves a debit to the term deposit account, making the presented TDR a form of debit voucher.

Oct/Nov 2017

25. Identify the correct statement regarding pay-in-slips.
(A) They are always presented in a standard format that cannot be customized by any special arrangement.
(B) They are primarily used by customers for the specific purpose of withdrawing money from their accounts.
(C) They are filled by depositors and borrowers to deposit funds and consequently serve as credit vouchers.
(D) They are exclusively used for depositing physical cash and not for cheques or other financial instruments.

Ans :

(C) They are filled by depositors and borrowers to deposit funds and consequently serve as credit vouchers.
Pay-in-slips are primary documents used by customers, including both depositors and borrowers, to deposit funds into their accounts. This deposit increases the account balance, resulting in a credit entry. Therefore, these slips function as credit vouchers. While generally standard, special formats can exist based on formal agreements with certain customers.

May/June 2014

26. Which of the following is a type of credit voucher in a bank?
(A) Applications submitted for the issuance of a Demand Draft, RTGS, or NEFT transfer.
(B) Cheques that are issued by customers for making payments from their accounts.
(C) Withdrawal forms received from customers for taking cash from savings accounts.
(D) Term deposit receipts that are presented by customers for premature closure and payment.

Ans :

(A) Applications submitted for the issuance of a Demand Draft, RTGS, or NEFT transfer.
When a customer applies for a Demand Draft, RTGS, or NEFT, they provide funds to the bank (either by cash, cheque, or debit to their account). The bank receives value, which is a credit. The application form itself acts as a credit voucher, evidencing the receipt of funds for issuing the instrument.

Oct/Nov 2018

27. Challans for deposits into accounts of the Central/State Government, such as for taxes or Public Provident Fund, are treated as:
(A) Debit vouchers
(B) Composite vouchers
(C) Internal memos
(D) Credit vouchers

Ans :

(D) Credit vouchers

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The text states that most transactions covered by composite vouchers pertain to the internal accounts of the bank, i.e., non-customer accounts. Examples include recording bills received for collection or guarantees issued by the branch. While they can be used for error rectification in customer accounts, their primary use is for internal transactions.

Oct/Nov 2024

63. The periodic preparation of a trial balance of personal ledgers and agreeing it with general ledger control accounts is an exercise referred to as:

(A) Balancing of books
(B) Daily closing
(C) Year-end closing
(D) System audit

Ans :

(A) Balancing of books
The term 'balancing of books' has a specific meaning in banking parlance. It describes the routine, periodic process (typically fortnightly) of extracting balances from all accounts in a subsidiary ledger, creating a trial balance, and reconciling the total with the balance of the corresponding control account in the General Ledger to ensure accuracy.

May/June 2024

64. Consider the following instruments:

1. Dividend/interest warrants issued by the bank's customers.
2. Drafts/pay orders issued by the branch itself that are cancelled.
3. Term deposit receipts presented for payment.
4. Pay-in-slips filled by customers.

Which of the above are considered debit vouchers?

(A) 1, 2, and 4 only
(B) 1, 3, and 4 only
(C) 1, 2, and 3 only
(D) 2, 3, and 4 only

Ans :

(C) 1, 2, and 3 only
Dividend/interest warrants, cancelled drafts/pay orders being refunded, and term deposit receipts presented for payment all result in a debit entry to an account (customer's liability, drafts payable, or term deposit liability). A pay-in-slip is for depositing money and is a credit voucher. Therefore, items 1, 2, and 3 are all debit vouchers.

Oct/Nov 2010

65. What is the chronological order of events in the 'voucher posting' system at the end of the day?

P. Vouchers are entered on separate voucher summary sheets.
Q. The total from summary sheets is posted to the respective control account in the general ledger.
R. Vouchers are posted to individual accounts in subsidiary ledgers.
S. The general ledger trial balance is prepared.

(A) R, P, Q, S
(B) P, R, Q, S
(C) R, Q, P, S
(D) P, Q, R, S

Ans :

(A) R, P, Q, S
The process starts with vouchers being posted straightaway to individual subsidiary ledger accounts (R). At the end of the day, these vouchers are aggregated on summary sheets (P). The totals from these sheets are then posted to the GL control accounts (Q). Finally, the GL trial balance is prepared (S).

May/June 2005

66. Which one of the following is NOT a credit voucher?

(A) Debit advice prepared by another branch for a realised collection instrument.
(B) Applications for issue of demand drafts.
(C) A copy of the collection schedule received from another branch for a paid instrument.
(D) Challans for deposits into a Public Provident Fund account.

Ans :

(A) Debit advice prepared by another branch for a realised collection instrument.
A debit advice received from another branch signifies that the other branch has debited your branch's account in its books. Your branch will use this advice as a debit voucher to debit the inter-office account and subsequently credit the customer. The other options all represent a credit to an account (government, customer, or internal).

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utility lies in handling any transaction with multiple debits and credits efficiently.

May/June 2017

32. A composite voucher would be most appropriate for which of the following transactions?
(A) A customer depositing cash into their savings account.
(B) Rectifying an erroneous debit to the current account ledger instead of the cash credit account ledger.
(C) A customer withdrawing cash using a cheque.
(D) Paying monthly interest to a single term deposit holder.

Ans :

(B) Rectifying an erroneous debit to the current account ledger instead of the cash credit account ledger.
A composite voucher records both debit and credit particulars. To rectify an error where a current account was wrongly debited instead of a cash credit account, a composite voucher is ideal. It will show a debit to the correct 'cash credit account' and a corresponding credit to the incorrect 'current account' to reverse the mistake.

Oct/Nov 2025

33. What is the primary purpose of having entries in personal ledgers checked by persons other than those who made them?
(A) To fulfill regulatory compliance as mandated by the central bank.
(B) To ensure the immediate detection of most clerical errors.
(C) To provide cross-functional training for new employees on verification procedures.
(D) To assess the performance and accuracy of the data entry staff for appraisals.

Ans :

(B) To ensure the immediate detection of most clerical errors.
The practice of having a second person check entries made by another is a fundamental internal control principle known as 'maker-checker' or four-eyes principle. Its main objective is to promptly identify and rectify clerical errors, such as incorrect amounts or posting to the wrong account, thereby maintaining the accuracy and integrity of the bank's books.

May/June 2007

34. The periodic exercise of preparing a trial balance of personal ledgers and agreeing it with general ledger control accounts is referred to as:
(A) Balancing of books
(B) Daily closing
(C) Year-end closing
(D) System audit

Ans :

(A) Balancing of books
'Balancing of books' in a banking context specifically refers to the periodic reconciliation process. This involves preparing a trial balance from the subsidiary personal ledgers (like savings or current account ledgers) and ensuring that the total balances agree with the figures in the corresponding control accounts in the General Ledger, which is typically done every two weeks.

Oct/Nov 2015

35. Why is it difficult to identify a single, uniform accounting system across all banks?
(A) Because banks are not regulated by a single accounting body and are free to choose their own standards.
(B) Because bank employees receive training in fundamentally different and often conflicting accounting methodologies.
(C) Because systems vary based on a bank's hardware, software, security needs, and transaction types.
(D) Because individual customers demand different types of accounting reports and statements from each bank.

Ans :

(C) Because systems vary based on a bank's hardware, software, security needs, and transaction types.
There is no one-size-fits-all accounting system for banks because each bank's system is tailored to its specific needs. Factors like hardware configuration, customized software capabilities, security levels, and the volume and nature of transactions processed lead to significant differences. Large banks often develop proprietary software to meet their unique operational and informational requirements.

May/June 2009

36. Which of the following factors influences the design of a bank's accounting system?

NODIA

When a customer deposits money for a government scheme or tax payment using a challan, the bank collects the money on behalf of the government. This amount is credited to the respective government account held with the bank. The challan, therefore, serves as a credit voucher for that specific government account.

May/June 2011

28. A credit voucher prepared by the branch on its printed stationery and authorized by an official is used for transactions like:
(A) Payment of a cheque to a customer.
(B) Crediting income like locker charges to an income account.
(C) Refunding a cancelled demand draft.
(D) Debiting a customer's account for standing instructions.

Ans :

(B) Crediting income like locker charges to an income account.
Banks prepare internal credit vouchers on their own stationery to record income. For instance, when locker charges are recovered, the amount is credited to the bank's 'Locker Rent Income' account. The internally generated, authorized credit voucher is the source document for this entry, reflecting an increase in the bank's income.

Oct/Nov 2013

29. When a bank collects payment for an instrument sent by another branch, the credit advice or a copy of the collection schedule sent to that branch is treated as a:
(A) Debit voucher by the collecting branch.
(B) Credit voucher by the collecting branch.
(C) Credit voucher by the sending branch.
(D) Debit voucher by the sending branch.

Ans :

(C) Credit voucher by the sending branch.
The collecting branch, upon receiving payment, will credit the sending branch's inter-office account. The advice it sends back informs the sending branch of this credit. The sending branch will then use this advice as a credit voucher to credit the customer's account for whom the instrument was collected, completing the transaction.

May/June 2020

30. What is the common practice in banks for handling debits or credits of a similar nature to a large number of accounts?
(A) Preparing an individual, separate voucher for each and every account that is affected.
(B) Making entries directly without vouchers and performing a reconciliation at the month's end.
(C) Sending notifications to customers to make the corresponding entries themselves through online banking.
(D) Preparing a single consolidated voucher that is supported by an attached list of all affected accounts.

Ans :

(D) Preparing a single consolidated voucher that is supported by an attached list of all affected accounts.
For transactions affecting numerous accounts in the same way, such as crediting periodic interest to depositors or debiting inspection charges, preparing individual vouchers is inefficient. Banks commonly use a single consolidated voucher. This master voucher is supported by a detailed list containing the specific accounts and the respective amounts to be debited or credited.

Oct/Nov 2009

31. **Assertion (A) :** Most transactions covered by composite vouchers pertain to the internal, non-customer accounts of the bank.
Reason (R) : Composite vouchers are primarily designed to rectify errors made in customer accounts.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(C) (A) is true but (R) is false.
Assertion (A) is true, as composite vouchers are frequently used for internal transactions like recording bills for collection or guarantees issued. However, Reason (R) is false. While composite vouchers can be used for error rectification, it is not their primary design purpose. Their main

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A's SB Account ₹2,000.

(D) Debit Mr. A's SB Account ₹2,000; Credit Interest Account ₹2,000.

Ans :

(A) Debit Cash Account ₹2,000; Credit Mr. A's SB Account ₹2,000.

When Mr. A deposits cash, the bank's cash holdings increase, so the Cash Account is debited. Simultaneously, the bank's liability to Mr. A increases, so his Savings Bank (SB) account is credited. This accurately reflects the transaction's impact on the bank's assets and liabilities according to the rules of double-entry bookkeeping.

Oct/Nov 2020

41. After processing this cheque deposit, what will be the balance in Mr. A's account and what type of entry is passed in his account?

(A) ₹6,000; the transaction is recorded as a transfer debit entry in his account.

(B) ₹16,000; the transaction is recorded as a standard cash credit entry in his account.

(C) ₹16,000; the transaction is recorded as a transfer credit entry in his account.

(D) ₹11,000; no change occurs until the cheque is cleared by an external bank.

Ans :

(C) ₹16,000; the transaction is recorded as a transfer credit entry in his account.

Since both Mr. A and Mr. B are customers of the same branch, this is an internal transfer. Mr. A's account is credited by ₹5,000, and Mr. B's account is debited by ₹5,000. This is a 'transfer credit' for Mr. A, increasing his balance from ₹11,000 to ₹16,000 (₹11,000 + ₹5,000).

May/June 2022

42. What is the impact of this clearing payment on Mr. A's account and the bank's books?

(A) Mr. A's account is credited by ₹3,000, and the clearing house account is debited.

(B) Mr. A's account is debited by ₹3,000.

(C) Mr. A's account is credited by ₹3,000, and the cash account is debited.

(D) Mr. A's account is debited by ₹3,000, and the clearing house account is credited.

Ans :

(A) Mr. A's account is credited by ₹3,000, and the clearing house account is debited.

When payment is received for a cheque deposited by a customer through clearing, it is a 'clearing-in' transaction. The customer's account is credited as funds are received. The corresponding debit is to the account of the bank that conducts the clearing house, settling the inter-bank obligation. Mr. A's balance becomes ₹19,000.

Oct/Nov 2012

43. How will this transaction be recorded in the bank's books?

(A) Credit Mr. A's account ₹4,000; Debit Clearing House account ₹4,000.

(B) Debit Mr. A's account ₹4,000; Credit Mr. C's account ₹4,000.

(C) Debit Cash account ₹4,000; Credit Mr. A's account ₹4,000.

(D) Debit Mr. A's account ₹4,000; Credit Clearing House account ₹4,000.

Ans :

(D) Debit Mr. A's account ₹4,000; Credit Clearing House account ₹4,000.

This is a 'clearing-out' transaction. The cheque was issued by the branch's customer, Mr. A. Therefore, his account must be debited to reflect the payment. The funds are being paid out through the clearing system, so the account of the bank conducting the clearing house is credited to settle the inter-bank payment obligation.

NODIA

May/June 2021

44. What are the corresponding debit and credit entries for this transaction?

(A) Debit Mr. A's account ₹6,000; Credit Cash account ₹6,000.

(B) Debit Mr. A's account ₹6,000; Credit Inter-Office account/Draft account ₹6,000.

(C) Debit Inter-Office account/Draft account ₹6,000; Credit Mr. A's account ₹6,000.

(D) Debit Draft account ₹6,000; Credit Commission account ₹6,000.

Ans :

(B) Debit Mr. A's account ₹6,000; Credit Inter-Office account/Draft account ₹6,000.

Mr. A is paying for the draft from his account, so his account is debited by ₹6,000. The bank is now liable to pay this amount at another branch. This liability is recorded by crediting an internal account, such as the 'Inter-Office account' or a specific 'Drafts Payable' account, until the draft is paid.

Oct/Nov 2005

45. What is the closing balance in Mr. A's SB account at the end of the day on February 28, 2022?
(A) ₹19,000
(B) ₹15,000
(C) ₹9,000
(D) ₹29,000

Ans :

(C) ₹9,000
The closing balance is calculated as: Opening Balance + Credits - Debits.
Credits = ₹2,000 (cash) + ₹5,000 (transfer) + ₹3,000 (clearing) = ₹10,000.
Debits = ₹4,000 (clearing) + ₹6,000 (draft) = ₹10,000.
Closing Balance = ₹9,000 (opening) + ₹10,000 (credits) - ₹10,000 (debits) = ₹9,000.

May/June 2008

46. From the perspective of Mr. B's account, what is the effect of this transaction?
(A) A transfer credit of ₹5,000.
(B) A cash debit of ₹5,000.
(C) A clearing debit of ₹5,000.
(D) A transfer debit of ₹5,000.

Ans :

(D) A transfer debit of ₹5,000.
Mr. B is the issuer of the cheque. When the cheque is processed, funds are moved out of his account to Mr. A's account. This is a non-cash transaction, so it is recorded as a 'transfer debit' in Mr. B's account, reducing his account balance by the cheque amount of ₹5,000.

Oct/Nov 2023

47. How are these totals reflected in the General Ledger (GL)?
(A) The SB control account in the GL is credited with ₹500,000 and debited with ₹450,000.
(B) Each of the day's transactions is individually posted to the SB control account in the GL.
(C) The SB control account in the GL is credited with only the net difference amount of ₹50,000.
(D) The totals are recorded only in the SB Day Book and are not posted to the GL until month-end.

Ans :

(A) The SB control account in the GL is credited with ₹500,000 and debited with ₹450,000.
The day's transactions are first summarized in the SB Day Book. The total credits and total debits from the Day Book are then posted to the respective columns of the Savings Bank (SB) control account in the General Ledger. This updates the master ledger with the aggregate movement for the day.

May/June 2013

48. Based on the provided text, how is this transaction typically handled in a computerized environment?
(A) A separate physical voucher is systematically prepared and printed for each individual account credited.
(B) No separate vouchers are prepared, as the transaction is automatically processed and recorded by the system.
(C) A single consolidated physical voucher is manually prepared to cover all the accounts affected.
(D) The branch manager personally prepares and signs a single credit voucher to authorize the transaction.

Ans :

(B) No separate vouchers are prepared, as the transaction is automatically processed and recorded by the system.
The text explicitly mentions that for system-triggered transactions like interest application, as well as ATM, internet, or mobile banking transactions, separate vouchers are not prepared. The core banking system is designed to automatically process and record these transactions, creating the necessary accounting entries without manual voucher generation, ensuring efficiency and automation.

Oct/Nov 2016

49. In this 'clearing-out' transaction, which account is credited by Mr. A's branch?
(A) Mr. A's account.
(B) The account of the bank conducting the clearing house.
(C) The cash account of the branch.
(D) The suspense account of the branch.

Ans :

(B) The account of the bank conducting the clearing house.
In a clearing-out transaction, the branch is paying money on behalf of its customer. The customer's

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account (Mr. A) is debited. The corresponding credit entry is made to the account of the bank that manages the clearing house. This credit settles the payment obligation of the branch within the inter-bank clearing system.

May/June 2018

50. What is the fundamental similarity in accountancy basics between a bank and any other business enterprise?

(A) The core principles of accountancy remain the same.
(B) The sequence of posting to journals and ledgers is identical.
(C) The types of vouchers used for all transactions are exactly the same.
(D) The frequency of preparing the trial balance is the same.

Ans :

(A) The core principles of accountancy remain the same.
Despite procedural differences, such as the timing of ledger posting, the basics of accountancy are universal. Banks, like any other enterprise, adhere to fundamental principles like the double-entry system, the use of debits and credits, and the ultimate goal of preparing financial statements to reflect a true and fair view of financial health.

Oct/Nov 2011

51. Which of the following is listed as a key term related to the operational aspects of accounting entries in banks?

(A) Capital Adequacy
(B) Risk Management
(C) Balancing of books
(D) Asset Classification

Ans :

(C) Balancing of books
'Balancing of books' refers to the specific banking practice of periodically preparing a trial balance of personal ledgers and agreeing it with the general ledger control accounts to ensure accuracy and reconciliation of records.

May/June 2025

52. Match List-I with List-II regarding types of vouchers.
List-I (Instrument)
P. Cheque issued by a customer
Q. Pay-in-slip for cash deposit
R. Application for issue of a term deposit
S. Withdrawal form from a savings account
List-II (Voucher Type)
1. Credit Voucher
2. Debit Voucher
(A) P-2, Q-1, R-1, S-2
(B) P-1, Q-2, R-2, S-1
(C) P-2, Q-2, R-1, S-1
(D) P-1, Q-1, R-2, S-2

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Ans :

(A) P-2, Q-1, R-1, S-2
A cheque issued by a customer and a savings account withdrawal form both result in a debit to the customer's account, making them debit vouchers (P-2, S-2). A pay-in-slip for a deposit and an application for a term deposit both represent receipt of funds by the bank, making them credit vouchers (Q-1, R-1).

Oct/Nov 2008

53. Consider the following statements about vouchers in banking:

1. There are two kinds of vouchers: one for debit/credit only, and another for both.
2. The latter kind, containing both debit and credit, is called a composite voucher.
3. Cheques issued by customers are an example of credit vouchers.

Which of the above statements is/are correct?
(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2 and 3

Ans :

(A) 1 and 2 only
Statements 1 and 2 are correct as they accurately define the types of vouchers, including the composite voucher. Statement 3 is incorrect because a cheque issued by a customer is an instruction to pay, leading to a debit from their account, and is therefore a debit voucher, not a credit voucher.

May/June 2010

54. Which of the following is NOT a broad category of debit vouchers?

(A) Drafts issued by other banks on the branch under a specific, pre-approved reciprocal arrangement.
(B) Challans used for making deposits into various accounts of the Central or State

(A) The specific geographical location and the architectural design of the bank's main headquarters building.
(B) The total number of employees in the IT department and their specific, individual programming skill sets.
(C) The accounting software choices and the marketing strategies that are currently being used by competing banks.
(D) The information needs of various stakeholders and the sheer volume and nature of the bank's daily operations.

Ans :

(D) The information needs of various stakeholders and the sheer volume and nature of the bank's daily operations.
A bank's accounting system is designed with key considerations in mind. These include the nature and sheer volume of its daily operations and, crucially, the information requirements of its stakeholders, which include management, regulators, auditors, and customers. The system must efficiently process transactions while generating necessary reports and data for these diverse groups.

Oct/Nov 2022

37. Which of the following statements is incorrect regarding the accounting systems in banks?
(A) Every big bank has customized banking software as per its own requirement.
(B) Accounting systems differ amongst different banks.
(C) All banks in a country are mandated to use identical, standardized accounting software.
(D) A bank's accounting system is designed keeping in view the nature and volume of its operations.

Ans :

(C) All banks in a country are mandated to use identical, standardized accounting software.
This statement is incorrect. While banks must follow standardized accounting principles and reporting formats prescribed by the regulator, they are not required to use identical software. Banks choose or develop their own core banking software based on their specific operational needs, scale, hardware, and strategic goals, leading to diverse systems across the industry.

May/June 2023

38. Based on the provided text, what are the two key financial statements that fulfill the ultimate objective of recording transactions?
(A) Cash Flow Statement and Trial Balance
(B) Balance Sheet and P&L Account
(C) General Ledger and Subsidiary Ledger
(D) Annual Report and Audit Report

Ans :

(B) Balance Sheet and P&L Account
The excerpt explicitly states that the ultimate objective of recording financial transactions is the preparation of the balance sheet and the P&L account. These two statements are identified as the means by which stakeholders receive a fair view of the company's operational results and its financial position at the end of the accounting period.

Oct/Nov 2006

39. According to the source, what is the correct sequence of recording a transaction in a bank's manual accounting system?
(A) Journal -> Control Account -> Physical Ledger
(B) Journal (Day Book) -> Physical Ledger -> General Ledger Control Account
(C) Control Account -> Journal -> Physical Ledger
(D) Physical Ledger -> Journal (Day Book) -> General Ledger Control Account

Ans :

(D) Physical Ledger -> Journal (Day Book) -> General Ledger Control Account
The provided text outlines a specific sequence for manual bank accounting. It clearly states that entries are first made in the physical ledgers. Afterward, these entries are summarized in the journal (day book). Finally, the total from the journal is posted to the relevant control account in the General Ledger, establishing a unique workflow.

May/June 2016

40. What is the accounting entry in the books of the bank for this cash deposit transaction?
(A) Debit Cash Account ₹2,000; Credit Mr. A's SB Account ₹2,000.
(B) Debit Mr. A's SB Account ₹2,000; Credit Cash Account ₹2,000.
(C) Debit Suspense Account ₹2,000; Credit Mr.

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(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
Both statements are factually correct. It is important for staff to know the manual system, and most bank branches are computerized. However, the reason for knowing the manual system is to understand the underlying process to answer queries, not simply because computerization has occurred. The two facts are related but one does not logically explain the other.

Oct/Nov 2021

59. A customer signs a letter of authority containing standing instructions to debit their account monthly for a loan installment. This letter acts as a:
(A) Standing credit voucher.
(B) Standing composite voucher.
(C) One-time advice note.
(D) Standing debit voucher.

Ans :

(D) Standing debit voucher.
A letter of authority with standing instructions provides the bank with ongoing permission to perform a specific transaction. In this case, the instruction is to debit the customer's account periodically. The letter itself serves as the authorization and is treated as a standing debit voucher, forming the basis for the recurring debit entries.

May/June 2012

60. When a bank prepares a credit voucher on its own stationery, for which of the following reasons might a customer's signature also be taken on it?
(A) To confirm that the bank's income from the transaction has been booked correctly in the GL.
(B) As evidence that a transaction, such as a deposit for non-judicial stamps, pertains to that customer.
(C) This is never done, as all internal vouchers are required to be signed exclusively by bank officials.
(D) To provide the necessary authorization for the specific bank official who prepared the voucher.

Ans :

(B) As evidence that a transaction, such as a deposit for non-judicial stamps, pertains to that customer.
While internal credit vouchers are normally signed only by bank officials, there are instances where a customer's signature is also obtained. This happens when the transaction directly involves the customer, such as when they deposit money for a specific purpose like purchasing non-judicial stamps. The signature serves as the customer's acknowledgement.

Oct/Nov 2007

61. Identify the correct pair from the following options.
(A) Cheque issued by customer - Credit Voucher
(B) Pay-in-slip for deposit - Debit Voucher
(C) Application for RTGS - Credit Voucher
(D) Withdrawal form - Composite Voucher

NODIA

Ans :

(C) Application for RTGS - Credit Voucher
An application for an RTGS transfer involves the customer giving funds to the bank for remittance. This receipt of funds by the bank is a credit transaction from the bank's perspective, making the application a credit voucher. All other pairs are incorrectly matched with their respective voucher types.

May/June 2019

62. Which of the following statements about a 'composite voucher' is correct?
(A) It is a specific type of voucher used only for cash transactions that involve multiple accounts.
(B) It is a simplified voucher that can only evidence a single debit and a single corresponding credit.
(C) It is simply another name for a consolidated voucher, which is used for mass transaction processing.
(D) It primarily pertains to non-customer, internal accounts of the bank, such as bills for collection.

Ans :

(D) It primarily pertains to non-customer, internal accounts of the bank, such as bills for collection.

Government.
(C) Letters of authority that are signed by customers and contain standing instructions for periodic debits.
(D) Term deposit receipts that are presented by the holder for renewal upon reaching their maturity date.

Ans :

(B) Challans used for making deposits into various accounts of the Central or State Government.
Challans for deposits into government accounts represent funds being paid into those accounts. This increases the balance of the government's account with the bank, resulting in a credit entry. Therefore, such challans are credit vouchers, not debit vouchers. All other options listed result in a debit to some account.

Oct/Nov 2019

55. Which of the following is an example of a credit voucher?
(A) A debit advice prepared by another branch confirming the realization of a collection instrument.
(B) A draft issued by the branch itself which is later cancelled at the customer's request for a refund.
(C) A traveller's cheque that was issued by any branch and is now presented at your branch for payment.
(D) An application form submitted by a customer for the purpose of issuing a new banker's cheque.

Ans :

(D) An application form submitted by a customer for the purpose of issuing a new banker's cheque.
An application for the issuance of a banker's cheque, pay order, or similar instrument involves the customer providing funds to the bank. The bank receives value, for which it will issue the instrument. This receipt of funds is recorded as a credit, making the application a credit voucher. The other options are all debit vouchers.

May/June 2015

56. What is the primary control mechanism to detect clerical errors immediately after entries are made in personal ledgers and summary sheets?
(A) Entries are checked by persons other than those who made them.
(B) Entries are checked by the branch manager at the end of the day.
(C) The computer system automatically flags any potential errors.
(D) Customers are asked to confirm the entries via SMS alerts.

Ans :

(A) Entries are checked by persons other than those who made them.
A fundamental internal control is the 'maker-checker' process. All entries made in personal ledgers and summary sheets are independently verified by another staff member. This separation of duties ensures that most clerical errors are caught and corrected promptly, enhancing the accuracy of the accounting records before they are further processed.

Oct/Nov 2014

57. Identify the incorrect statement regarding accounting operations in a bank.
(A) The general ledger trial balance is prepared at the conclusion of business every day.
(B) All transactions occurring in a bank can be classified into two main types: cash and non-cash.
(C) In manual operations, entries are first posted in the day book and subsequently in the ledger.
(D) A composite voucher is a valid instrument that can be used for rectifying an accounting error.

Ans :

(C) In manual operations, entries are first posted in the day book and subsequently in the ledger.
The statement that entries are first posted in the day book is incorrect for manual banking operations. A peculiar feature of bank accounting is that entries are first recorded in the individual customer or subsidiary ledgers. Only after this are the transactions summarized in the day book (journal) for posting to the General Ledger.

May/June 2006

58. **Assertion (A) :** It is imperative for bank staff to understand the manual system of accounting.
Reason (R) : Most banks in the country have now computerized all or most of their branches.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).

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Oct/Nov 2017

67. The need for customer ledger accounts to be accurate and up-to-date is significantly stronger in banks than in other enterprises primarily because:

(A) Banks typically have a much larger daily volume of transactions than most other types of businesses.

(B) Bank accounting is now fully computerized, which automatically allows for instant and error-free updates.

(C) Banks cannot afford inaccuracies and must reflect every transaction instantly to maintain customer trust.

(D) Bank auditors are known to be more stringent and demand a higher level of accuracy than other auditors.

Ans :

(C) Banks cannot afford inaccuracies and must reflect every transaction instantly to maintain customer trust.

The core of a bank's relationship with its customers is the management of their funds. Any delay or inaccuracy in updating a customer's account can lead to financial loss, customer dissatisfaction, and loss of trust. Therefore, the imperative to maintain perfectly accurate and real-time ledgers is much more critical than in non-financial enterprises.

May/June 2014

68. If a bank branch pays for an instrument like a traveller's cheque of another bank under an approved arrangement, the instrument itself acts as a:

(A) Credit voucher

(B) Composite voucher

(C) Non-negotiable advice

(D) Debit voucher

Ans :

(D) Debit voucher

When the branch pays for an instrument issued by another bank, it debits an account to reflect the payment made on behalf of that bank (e.g., a nostro account or a specific clearing account). The physical instrument presented for payment serves as the authenticating document for this debit entry, thus functioning as a debit voucher.

Oct/Nov 2018

69. Match the transaction type in List-I with the account affected in List-II.

List-I (Transaction)

P. Customer 'A' deposits a draft drawn on the branch.

Q. Bank pays interest on deposit accounts.

R. Customer 'A' deposits a cheque drawn by customer 'B' (same branch).

S. Customer deposits cash into their account.

List-II (Account Debited)

1. Customer 'B' account
2. Cash account
3. 'Draft' account (internal)
4. 'Interest Account' (internal)

(A) P-3, Q-4, R-1, S-2

(B) P-4, Q-3, R-2, S-1

(C) P-3, Q-1, R-4, S-2

(D) P-2, Q-4, R-1, S-3

Ans :

(A) P-3, Q-4, R-1, S-2

P: When a draft is paid, the internal 'Draft' account is debited. Q: Payment of interest is an expense, so the 'Interest Account' is debited. R: In an internal transfer, the cheque issuer's (Customer 'B') account is debited. S: When cash is deposited, the bank's 'Cash' account is debited as its assets increase.

May/June 2011

70. Which of the following statements is/are correct?

Statement I : In modern accounting, every credit/debit accounting entry must have one or more corresponding debit/credit entries.

Statement II : A single financial transaction can affect more than two accounts in the ledger.

(A) Only Statement I is correct.

(B) Only Statement II is correct.

(C) Both Statement I and Statement II are correct.

(D) Neither Statement I nor Statement II is correct.

Ans :

(C) Both Statement I and Statement II are correct. Both statements correctly describe the double-entry system. Statement I explains the core principle that no entry is standalone. Statement II is also correct, as a transaction can be compound, involving one debit and multiple credits, or vice-versa, thus affecting more than two accounts while still maintaining the debit-credit balance.

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(D) Debit voucher

When your branch pays such an instrument, it is making a payment on behalf of the issuing bank. This payment is recorded as a debit to an inter-bank account or a specific suspense account pending settlement. The paid instrument itself serves as the physical proof and authorization for this debit entry.

May/June 2008

88. Consider the following:

I. A customer deposits cash of ₹50,000.

II. The bank debits the Cash account and credits the Customer account.

Which of the following is correct?

(A) I is the cause, and II is the effect.

(B) II is the cause, and I is the effect.

(C) I and II are independent actions.

(D) I and II are effects of a common cause.

Ans :

(A) I is the cause, and II is the effect.

The customer's action of depositing cash (I) is the financial transaction or the cause. The bank's accounting entry to debit the Cash account and credit the Customer account (II) is the recording of that transaction, which is the effect. The accounting entry reflects the business event that has taken place.

Oct/Nov 2023

89. A bank credits periodic interest to a large number of savings account holders. What is the most efficient way to document this in a manual or semi-automated system?

(A) Prepare one credit voucher for each customer.

(B) Simply make the entries in the ledgers without any voucher.

(C) Prepare a consolidated credit voucher with an attached list of accounts and amounts.

(D) Prepare a single composite voucher debiting interest and crediting cash.

Ans :

(C) Prepare a consolidated credit voucher with an attached list of accounts and amounts.

For mass credits of a similar nature, preparing individual vouchers is highly inefficient. The standard practice is to use a single consolidated voucher for the total amount. This voucher is then supported by a detailed schedule or list that specifies each individual account number and the corresponding interest amount to be credited.

May/June 2013

90. The practice of posting entries first to ledgers and then to journals in banks is a departure from standard accounting. What does this practice ensure?

(A) Immediate accuracy and up-to-date status of customer accounts.

(B) Faster preparation of the final balance sheet.

(C) Easier tax computation for the bank.

(D) Compliance with international banking laws.

Ans :

(A) Immediate accuracy and up-to-date status of customer accounts.

The primary driver for this procedural peculiarity is the critical need to have customer account balances correct and current at all times. By posting directly to the customer's ledger, the bank ensures that the balance reflects the transaction instantly, which is paramount for customer service and operational integrity in banking.

Oct/Nov 2016

91. Which of the following is an example of a 'transfer transaction'?

(A) A customer withdrawing ₹10,000 cash from their account.

(B) A customer depositing ₹20,000 in cash.

(C) The bank paying electricity bill in cash.

(D) A customer depositing a cheque of ₹5,000 drawn by another customer of the same branch.

Ans :

(D) A customer depositing a cheque of ₹5,000 drawn by another customer of the same branch.

A 'transfer transaction' is a non-cash transaction. When a cheque drawn on one customer of the branch is deposited by another customer of the same branch, no physical cash is involved. It is a simple transfer of funds between two accounts within the branch's books, making it a classic example of a transfer transaction.

NODIA

May/June 2018

92. Which of the following is NOT a valid reason for the accounting systems to differ among various banks?

(A) Differences in hardware configuration.

(B) Differences in the basic principles of double-entry accounting.

(C) Differences in software capabilities.

(D) Differences in the nature and volume of

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Oct/Nov 2025

75. In a computerized environment, which of the following operations is NOT automatically performed by the system after an authenticated entry is made?

(A) Automatically affecting the relevant day books with the transaction details.

(B) Automatically affecting the corresponding control accounts in the General Ledger (GL).

(C) Automatically including the transaction data in the preparation of financial statements.

(D) Subsequent physical authentication of the original source voucher by a designated officer.

Ans :

(D) Subsequent physical authentication of the original source voucher by a designated officer.

After an entry is made and digitally authenticated by an official, the computerized system automatically handles subsequent processes like updating day books, the GL, and even generating financial statements. The authentication itself is done within the system; there is no subsequent physical authentication of a source voucher as part of the automated process.

May/June 2007

76. Based on the text, what is the immediate first step in the 'voucher posting' procedure after a voucher is created?

(A) It is entered on a voucher summary sheet.

(B) It is posted straightaway to the individual account in the subsidiary ledger.

(C) It is posted to the control account in the general ledger.

(D) It is filed and stored for end-of-day batch processing.

Ans :

(B) It is posted straightaway to the individual account in the subsidiary ledger.

The excerpt explicitly defines 'voucher posting' as the procedure where vouchers are "straightaway posted to the individual accounts in the subsidiary ledgers." This immediate posting to the customer-level or specific account ledger is the defining first action in this accounting method, ensuring that individual account balances are updated promptly.

Oct/Nov 2015

77. According to the provided text, what two components are agreed with each other during the 'balancing of books' exercise?

(A) The daily cash book balance and the physical cash balance held in the vault.

(B) The grand totals from the day book and the closing balances from the general ledger trial balance.

(C) The trial balance of personal ledgers and their corresponding general ledger control accounts.

(D) The balances in individual customer passbooks and the bank's internal ledger records for those customers.

Ans :

(C) The trial balance of personal ledgers and their corresponding general ledger control accounts.

The text clearly states that 'balancing of books' involves preparing a trial balance of the personal (subsidiary) ledgers. This trial balance is then "agreed with" the corresponding general ledger control accounts. This reconciliation ensures that the detailed subsidiary records are in sync with the master control accounts, verifying bookkeeping accuracy.

May/June 2009

78. Based on the excerpt, a composite voucher is suitable for which two distinct purposes?

(A) For recording both cash deposits and subsequent cash withdrawals from the same account.

(B) For simultaneously issuing new demand drafts and paying out matured fixed deposits.

(C) For posting periodic interest credits and debiting applicable service charges to customer accounts.

(D) For recording internal/non-customer transactions and for rectifying various types of accounting errors.

Ans :

(D) For recording internal/non-customer transactions and for rectifying various types of accounting errors.

The source provides two clear use cases for composite vouchers. First, it lists examples of internal, non-customer transactions like bills for collection, LCs, and guarantees. Second, it explicitly states that such vouchers can also be

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now be credited. A composite voucher would show both these actions.

Oct/Nov 2019

97. In the context of the illustration, the purchase of a draft for ₹6,000 by Mr. A leads to a debit in his account. What is the corresponding credit entry?
(A) Credit to the cash account of the branch.
(B) Credit to the Inter-Office account/Draft account.
(C) Credit to the account of the outstation branch.
(D) Credit to Mr. A's loan account.

Ans :

(B) Credit to the Inter-Office account/Draft account.
When the draft is issued, the branch incurs a liability to pay the amount at the specified outstation branch. This liability is recorded internally by crediting a specific account, which is referred to as the Inter-Office account or Drafts Payable account. This account is cleared when the draft is eventually paid.

May/June 2015

98. The accounting entry for a financial transaction is always expressed in terms of:
(A) Number of monetary units.
(B) Percentage points.
(C) A ratio or proportion.
(D) A descriptive narrative only.

Ans :

(A) Number of monetary units.
A fundamental principle of accounting is the money measurement concept. All financial transactions are recorded in the books of an enterprise in terms of monetary units, such as Rupees, Dollars, etc. This allows for a common, quantifiable basis for recording and reporting diverse economic events like sales, purchases, or payments.

Oct/Nov 2014

99. Most of the accounting functions in a modern bank, except for the original entry, are taken over by the computer system. What does 'original entry' refer to in this context?
(A) The final entry in the balance sheet.
(B) The first entry made in the General Ledger.
(C) The initial input of the transaction data at the branch level.
(D) The entry in the annual report.

Ans :

(C) The initial input of the transaction data at the branch level.
The 'original entry' refers to the very first step where the transaction is captured in the system. This is typically done by the branch staff (e.g., a teller entering a cash deposit). Once this initial data is entered and authenticated, the computerized system automatically handles all subsequent steps like posting, summarization, and reporting.

NODIA

May/June 2006

100. Which of the following is a debit voucher prepared by the branch on its printed stationery?
(A) A pay-in-slip for a cash deposit.
(B) A challan for tax payment.
(C) An application for a demand draft.
(D) A voucher for debiting an account based on a customer's standing instruction.

Ans :

(D) A voucher for debiting an account based on a customer's standing instruction.
When the bank acts on a standing instruction to debit a customer's account (e.g., for an insurance premium payment), it prepares an internal debit voucher. This voucher, prepared on the bank's stationery and authorized by an official, cites the standing instruction as its authority and serves as the source document for the debit.

Oct/Nov 2021

101. Which of the following is NOT a key feature of the 'voucher posting' system in banks?
(A) Vouchers are posted straightaway to individual accounts in subsidiary ledgers.
(B) Voucher totals are posted to control accounts in the general ledger.
(C) Vouchers are first entered in a journal before any ledger posting.
(D) The general ledger trial balance is prepared every day.

Ans :

(C) Vouchers are first entered in a journal before any ledger posting.
The defining characteristic of 'voucher posting' is that it bypasses the initial journal entry. Vouchers are posted directly to the subsidiary ledgers. The journal (or day book/summary sheet) is created

(C) A cash deposit made over the counter with a teller.
(D) System-triggered application of interest on savings accounts.

Ans :

(C) A cash deposit made over the counter with a teller.
The text explicitly lists several transaction types for which vouchers are not prepared because they are system-driven (ATM, internet banking, etc.). A cash deposit made over the counter with a teller is an originated transaction that is not on this list and would be initiated by the teller based on a physical pay-in-slip (a credit voucher).

May/June 2022

84. Consider the following statements regarding accounting systems in banks:
1. Accounting systems of different banks are largely identical due to industry standards.
2. A bank's accounting system design is influenced by the information needs of its stakeholders.
3. Every large bank typically uses customized banking software.

Which of the above statements is/are correct?
(A) 1 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2 and 3

Ans :

(B) 2 and 3 only
Statement 1 is incorrect; systems vary significantly. Statement 2 is correct, as stakeholder information needs are a key design factor. Statement 3 is also correct, as large banks often have customized software to meet their specific, large-scale requirements. Therefore, only statements 2 and 3 are correct.

Oct/Nov 2012

85. If a customer deposits a cheque of ₹10,000 drawn on another bank in a different city, which of the following vouchers would eventually be used by the customer's branch to credit their account upon realization?
(A) A new debit voucher prepared internally by the customer's home branch upon realization.
(B) A composite voucher that details both the collected amount and the applicable collection charges.
(C) A credit advice received from the collecting branch that confirms the receipt of funds.
(D) A fresh pay-in-slip that is signed again by the customer to authorize the credit.

Ans :

(C) A credit advice received from the collecting branch that confirms the receipt of funds.
The cheque is sent for collection. Once the other branch collects the funds, it sends a credit advice to the customer's home branch. This credit advice serves as the credit voucher for the home branch to finally credit the customer's account with the proceeds of the realised cheque.

May/June 2021

86. Which statement best describes the role of the General Ledger (GL) in a bank branch?
(A) It contains the complete and detailed transaction history of every individual banking customer.
(B) It contains control accounts whose totals are used to prepare the balance sheet and P&L account.
(C) It is a daily summary that completely replaces the need for any detailed subsidiary ledgers.
(D) It is considered a book of prime entry where all branch transactions are first recorded.

Ans :

(B) It contains control accounts whose totals are used to prepare the balance sheet and P&L account.
The General Ledger is the master ledger. It does not contain individual customer details but rather summary-level control accounts (e.g., Total Savings Deposits, Total Loans). The balances in these GL accounts are the ultimate figures used to construct the bank's trial balance, from which the P&L account and balance sheet are prepared.

Oct/Nov 2005

87. An instrument like a traveller's cheque or gift cheque of another bank is paid by your branch in terms of an approved arrangement. This instrument acts as a:
(A) Credit voucher
(B) Contra voucher
(C) Liability voucher
(D) Debit voucher

Ans :

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Oct/Nov 2013

71. Identify the incorrect pair.

(A) Cheques issued by the bank - Debit Voucher

(B) Drafts issued by other branches payable at the branch - Debit Voucher

(C) Withdrawal forms from savings bank - Debit Voucher

(D) Applications for issue of gift cheques - Debit Voucher

Ans :

(D) Applications for issue of gift cheques - Debit Voucher

An application for the issue of a gift cheque is a request for the bank to create a payment instrument. The customer provides funds for this. The bank's receipt of these funds is a credit. Therefore, the application is a credit voucher, not a debit voucher. The other pairs are correctly identified.

May/June 2020

72. A debit voucher prepared by the branch on its printed stationery. This voucher must be authorized by a designated official and may also require customer authority if:

(A) The debit is to the customer's account for a special, non-routine purpose.

(B) The debit is for a standard, pre-disclosed bank service charge like account maintenance fees.

(C) The debit is to an internal bank expense account, such as the 'Salaries Payable' account.

(D) The debit is for the purpose of rectifying a previous clerical error made by the bank's staff.

Ans :

(A) The debit is to the customer's account for a special, non-routine purpose.

While a bank official's authorization is standard for internal vouchers, additional authority is needed when the transaction affects a customer directly. If the voucher is for a debit to a customer's account (e.g., for a service not covered by standing instructions), the customer's authority or signature may also be required on the voucher.

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Oct/Nov 2009

73. What is the primary reason banks use consolidated vouchers for transactions like crediting monthly interest to numerous depositors?

(A) To reduce the total amount of paper used by the branch, supporting its environmental goals.

(B) To intentionally make the process more difficult for auditors to check each individual entry.

(C) To significantly improve the efficiency of processing a very large number of similar entries.

(D) To comply with a specific and explicit regulatory mandate on using consolidated voucher types.

Ans :

(C) To significantly improve the efficiency of processing a very large number of similar entries.

The main driver for using consolidated vouchers is efficiency. For mass transactions like periodic interest payments or charge debits affecting hundreds or thousands of accounts, creating individual vouchers is extremely time-consuming and impractical. A single consolidated voucher with a supporting list streamlines the process of authorization and posting significantly.

May/June 2017

74. Which of the following is the most accurate description of the information flow in a manual banking system?

(A) Transaction -> Subsidiary Ledger -> Day Book -> General Ledger

(B) Transaction -> Day Book -> General Ledger -> Subsidiary Ledger

(C) Transaction -> General Ledger -> Subsidiary Ledger -> Day Book

(D) Transaction -> Subsidiary Ledger -> General Ledger -> Day Book

Ans :

(A) Transaction -> Subsidiary Ledger -> Day Book -> General Ledger

In a bank's manual system, a transaction is first posted to the specific subsidiary ledger account (e.g., a customer's savings account). These entries are then aggregated in the Day Book (journal). Finally, the totals from the Day Book are posted to the control accounts in the General Ledger.

transactions processed.

Ans :

(B) Differences in the basic principles of double-entry accounting.
While banks use different hardware, software, and have varying transaction volumes, they all must adhere to the fundamental principles of accounting, such as the double-entry system. These principles are universal. The differences lie in the technological and procedural implementation, not in the core accounting theory itself.

Oct/Nov 2011

93. A customer presents a term deposit receipt for premature closure. This instrument acts as a debit voucher to which account?
(A) The customer's savings account.
(B) The bank's interest income account.
(C) The Term Deposit liability account.
(D) The cash account.

Ans :

(C) The Term Deposit liability account.
A term deposit is a liability for the bank. When it is closed prematurely, the bank's liability with respect to that specific deposit is extinguished. To record this, the Term Deposit liability account must be debited. The presented receipt is the authorization for this debit entry.

May/June 2025

94. **Assertion (A) :** The general ledger trial balance in a bank is prepared every day.
Reason (R) : This allows for the daily reconciliation of subsidiary ledger totals with their control accounts.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(C) (A) is true but (R) is false.
Assertion (A) is true; banks prepare the GL trial balance daily to ensure books are balanced. However, Reason (R) describes 'balancing of books', which is the periodic (e.g., fortnightly) reconciliation of subsidiary ledgers with control accounts. The daily GL trial balance simply confirms that total debits equal total credits in the General Ledger itself.

Oct/Nov 2008

95. What is the key distinction between a simple voucher and a composite voucher?
(A) A simple voucher evidences only a debit or credit, while a composite voucher contains both.
(B) A simple voucher is used exclusively for cash transactions, while a composite voucher is for non-cash.
(C) A simple voucher is always prepared by the customer, while a composite voucher is from the bank.
(D) A simple voucher needs only one signature, while a composite voucher always requires two.

Ans :

(A) A simple voucher evidences only a debit or credit, while a composite voucher contains both.
The fundamental difference lies in their structure. A simple voucher is one-sided, documenting either a debit to an account or a credit to an account. A composite voucher is two-sided, documenting a complete transaction with both its debit and credit aspects affecting different accounts on a single form.

May/June 2010

96. If a bank erroneously credits a customer's savings account instead of their current account, how would a composite voucher be used to rectify this?
(A) It would show a debit to the current account and a credit to the savings account.
(B) It would show a debit to the savings account and a credit to the current account.
(C) It would show a debit to cash and a credit to the current account.
(D) It would show a debit to the savings account and a credit to cash.

Ans :

(B) It would show a debit to the savings account and a credit to the current account.
To correct the error, the incorrect entry must be reversed, and the correct entry must be made. The savings account was wrongly credited, so it must be debited to reverse the entry. The current account, which should have been credited, must

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prepared to rectify errors, providing a specific example of correcting a mis-posted debit between two accounts.

Oct/Nov 2022

79. As per the text, when your branch receives a credit advice from another branch regarding a paid collection instrument, this advice serves as a credit voucher for what purpose?
(A) To pass the collected funds by crediting the account of the customer who initiated the collection.
(B) To credit the amount of commission earned by the bank into its own income account.
(C) To make a balancing entry by crediting the temporary inter-branch suspense account.
(D) To credit the General Ledger control account for savings deposits directly with the collected amount.

Ans :

(A) To pass the collected funds by crediting the account of the customer who initiated the collection.
The collection instrument was sent on behalf of a customer. The credit advice from the paying branch confirms receipt of funds. Your branch uses this advice as a credit voucher to pass the collected funds to your customer by crediting their account, thus completing the collection process for the customer.

May/June 2023

80. The excerpt suggests that the primary reason for differences in bank accounting functions is the need for:
(A) The constant pressure from shareholders to achieve higher levels of annual profitability.
(B) The critical need for immediate and accurate updating of individual customer accounts.
(C) The increasingly complex and strict regulatory compliance requirements imposed by central banks.
(D) The necessity of generating complex and detailed financial reports for international bodies.

Ans :

(B) The critical need for immediate and accurate updating of individual customer accounts.
The text directly attributes the difference in accounting functions to one specific requirement: "the need of updating the account of the customer as soon as or immediately after the transaction takes place." This emphasis on real-time, accurate customer account maintenance is highlighted as the core driver behind the peculiar procedures found in bank accounting.

Oct/Nov 2006

81. According to the text, when a customer purchases a draft by debiting their account, which internal account does the bank credit?
(A) Commission Account
(B) Inter-Office account / Draft account
(C) Suspense Account
(D) Cash Account

Ans :

(B) Inter-Office account / Draft account
The provided text explicitly states the accounting entry for purchasing a draft. It specifies that while the customer's account is debited, the corresponding credit entry is passed to the "Inter-Office account/ Draft account". This internal liability account represents the bank's obligation to pay the draft at the drawee branch.

May/June 2016

82. Based on the description of a 'clearing-out' transaction, when a cheque issued by a customer is paid via clearing, the credit entry is passed to which account?
(A) The account of the bank conducting the clearing house.
(B) The customer's account.
(C) The cash account.
(D) The suspense account.

Ans :

(A) The account of the bank conducting the clearing house.
The source describes a 'clearing-out' transaction where a cheque issued by the customer is paid. It clearly states that the customer's account is debited, and the corresponding credit entry is made to "the account of the bank conducting the clearing house." This settles the inter-bank fund transfer through the clearing system.

Oct/Nov 2020

83. According to the text, which of the following transactions would require a manually prepared voucher in a computerized bank?
(A) A cash withdrawal from an ATM.
(B) A fund transfer done via Mobile Banking.

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afterwards from these vouchers. Therefore, the statement that vouchers are first entered in a journal is incorrect for this system.

May/June 2012

102. When a customer deposits a draft drawn on the branch, which internal account of the bank is debited?
(A) Cash Account
(B) Draft Account
(C) Customer's Account
(D) Interest Account

Ans :

(B) Draft Account
When the draft was initially issued (by another branch or the same branch), a credit was made to a liability account like 'Drafts Payable'. When this draft is now presented for payment upon deposit, the bank's liability is extinguished. This is recorded by debiting the 'Draft Account' or 'Drafts Payable' account.

Oct/Nov 2007

103. Consider the following statements:
1. All entries in personal ledgers are checked by persons other than those who made them.
2. A trial balance of personal ledgers is prepared periodically, usually every two weeks.
3. The exercise of agreeing the personal ledger trial balance with GL control accounts is called 'voucher posting'.

Which of the above statements are correct?
(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2 and 3

Ans :

(A) 1 and 2 only
Statement 1 describes the maker-checker control. Statement 2 describes the frequency of preparing the subsidiary ledger trial balance. Both are correct. Statement 3 is incorrect; this exercise is called 'balancing of books', not 'voucher posting'. 'Voucher posting' is the process of posting vouchers directly to subsidiary ledgers.

May/June 2019

104. Which of the following best explains why a bank's accounting system needs to be robust and customized?
(A) To handle a large volume and diverse nature of transactions while meeting stakeholder information needs.
(B) To ensure that all banks have the exact same software for interoperability.
(C) To reduce the number of employees required in the accounting department.
(D) To eliminate the need for any manual intervention or oversight.

Ans :

(A) To handle a large volume and diverse nature of transactions while meeting stakeholder information needs.
A bank's accounting system must be specifically designed and often customized because it needs to process a high volume of varied transactions (cash, transfers, clearing, etc.) efficiently and securely. At the same time, it must generate accurate and timely information for a wide range of stakeholders, including management, regulators, and customers.

Oct/Nov 2024

105. In the illustration for Mr. A's account, what is the nature of the transaction "By transfer ₹5,000"?
(A) Deposit of a cheque drawn on another bank.
(B) Cash deposited by a third party into Mr. A's account.
(C) Deposit of a cheque drawn on another customer of the same branch.
(D) Inward remittance received via NEFT.

Ans :

(C) Deposit of a cheque drawn on another customer of the same branch.
The detailed explanation for this transaction specifies that it was a deposit of a cheque issued on the same branch by another customer, Mr. B. Since it doesn't involve cash or another bank, it's processed as an internal 'transfer' between the accounts of Mr. B and Mr. A.

May/June 2024

106. In the illustration, the entry "To clearing ₹4,000" represents a debit to Mr. A's account. What does this transaction signify?
(A) A cheque of ₹4,000 issued by Mr. A was presented and paid through clearing.
(B) Mr. A deposited a cheque of ₹4,000 which was cleared.
(C) The bank debited Mr. A's account for clearing charges of ₹4,000.
(D) Mr. A received an outward remittance of

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₹4,000.

Ans :

(A) A cheque of ₹4,000 issued by Mr. A was presented and paid through clearing.
A debit entry in a customer's account signifies an outflow of funds. The particular "To clearing" combined with the explanation of a 'clearing-out' transaction indicates that a cheque previously issued by Mr. A to someone else has now been presented to his bank through the clearing house mechanism and has been paid.

Oct/Nov 2010

107. The entry "By clearing ₹3,000" in Mr. A's account statement signifies:
(A) A cheque issued by Mr. A for ₹3,000 has been paid.
(B) A cash deposit of ₹3,000 was wrongly classified as clearing.
(C) A debit of ₹3,000 for clearing services.
(D) A cheque deposited by Mr. A for ₹3,000 has been realised.

Ans :

(D) A cheque deposited by Mr. A for ₹3,000 has been realised.
The entry is a credit ("By") to Mr. A's account. The particular "clearing" indicates the source of funds is the inter-bank clearing system. This means a cheque that Mr. A had previously deposited (an outstation cheque) has now been successfully collected, and the funds are being credited to his account.

May/June 2005

108. At the end of the day, the credit and debit summations of the SB Day Book are entered in the respective columns of which account?
(A) The Cash Book.
(B) The SB control account in the GL.
(C) The individual customer accounts.
(D) The Branch P&L account.

Ans :

(B) The SB control account in the GL.
The Day Book serves as a summary of all transactions for a specific ledger type (like Savings Bank). The total debits and total credits from this Day Book are then posted to the corresponding control account (SB control account) in the General Ledger (GL) to update the master financial records of the branch.

Oct/Nov 2017

109. Which of the following is an example of a transaction covered by a composite voucher that pertains to internal bank accounts?
(A) A customer depositing cash.
(B) A customer withdrawing cash.
(C) Recording 'Bills Received for Collection'.
(D) Crediting interest to a customer's savings account.

Ans :

(C) Recording 'Bills Received for Collection'.
'Bills Received for Collection' is a transaction that creates a contingent liability and asset for the bank. It is an internal accounting entry and does not immediately affect a customer's balance. The text specifically cites this as an example of a transaction covered by a composite voucher pertaining to internal accounts.

May/June 2014

110. The ultimate objective of recording financial transactions is to provide a 'fair picture' to stakeholders. Who are considered stakeholders in this context?
(A) Only the shareholders and owners of the enterprise.
(B) Only the management and employees of the enterprise.
(C) Only the government and tax authorities.
(D) A wide group including management, investors, customers, regulators, and auditors.

Ans :

(D) A wide group including management, investors, customers, regulators, and auditors.
Stakeholders are any individuals or groups with an interest in the enterprise's performance and financial position. This is a broad category that includes not just owners but also management for decision-making, customers and creditors for assessing stability, and regulators and auditors for ensuring compliance and fairness in reporting.

Oct/Nov 2018

111. What does the term 'Day Book' refer to in the context of bank accounting?
(A) A book summarizing all transactions of a particular ledger head for a day, synonymous with a journal.
(B) The General Ledger of the branch.
(C) A diary kept by the branch manager.

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(D) A record of employee attendance.

Ans :

(A) A book summarizing all transactions of a particular ledger head for a day, synonymous with a journal.
The text uses 'journal (day book)' interchangeably. In bank accounting, after entries are made in individual ledgers, they are summarized by ledger type (e.g., Savings Bank, Current Account) in a Day Book. This book acts as a journal for that category, providing daily totals for posting to the General Ledger.

May/June 2011

112. A debit voucher prepared by the branch on its printed stationery for debit to a customer's account requires authorization from a designated official. What is the primary purpose of this authorization?
(A) To ensure the customer has sufficient balance.
(B) To serve as an internal control, verifying the legitimacy and correctness of the transaction.
(C) To inform the customer about the debit.
(D) To get approval from the head office.

Ans :

(B) To serve as an internal control, verifying the legitimacy and correctness of the transaction.
The signature of an authorized official on a voucher acts as a crucial internal control. It signifies that a responsible person has reviewed the transaction, confirmed its validity and accuracy, and approved its processing. This prevents unauthorized or erroneous debits and maintains the integrity of the accounting process.

Oct/Nov 2013

113. Which of the following transactions would result in a debit to an internal account of the bank?
(A) A customer deposits cash.
(B) The bank pays interest on a savings deposit.
(C) A customer deposits a cheque drawn on another customer of the same branch.
(D) A customer withdraws cash.

Ans :

(B) The bank pays interest on a savings deposit.
Paying interest is an expense for the bank. This expense is recorded by debiting an internal nominal account, the 'Interest Account'. A cash deposit debits cash (asset), an internal transfer debits another customer's account (liability), and a cash withdrawal credits cash (asset). Only the interest payment debits an internal expense account.

May/June 2020

114. If a bank branch pays a dividend warrant issued by one of its corporate customers, the paid warrant serves as a:
(A) Debit voucher, debiting the customer's account.
(B) Credit voucher, crediting the customer's account.
(C) Composite voucher, debiting cash and crediting the customer.
(D) Memo, with no immediate accounting entry.

Ans :

(A) Debit voucher, debiting the customer's account.
The dividend warrant is an instruction from the corporate customer to the bank to pay the specified amount to the holder. When the bank makes this payment, it does so from the funds in the customer's account. Therefore, the customer's account is debited, and the paid warrant acts as the debit voucher.

Oct/Nov 2009

115. The process of checking entries made by one person by another person is a control measure designed to detect:
(A) Management fraud.
(B) Systemic software bugs.
(C) Clerical errors.
(D) Forged customer signatures.

Ans :

(C) Clerical errors.
The 'maker-checker' principle, where one person's work is reviewed by another, is primarily aimed at catching unintentional mistakes made during data entry or processing. This includes errors like typing the wrong amount, posting to the wrong account, or misinterpreting a voucher. It is a fundamental control against common clerical errors.

May/June 2017

116. The double-entry system implies that for a transaction involving a ₹5,000 credit to one account, there must be:
(A) A single debit of ₹5,000 to another account.

NODIA

(C) A software tool that automatically matches entries between the bank's ledger and the RBI statement.
(D) A regulatory requirement for dual signatures on all high-value cheques.

Ans :

(B) A process for preparing the reconciliation statement and subsequently clearing reconciling items.
The 'maker checker' concept is a principle of internal control applied to the reconciliation process. It involves one person (the maker) preparing the reconciliation statement by comparing the bank's books with the RBI statement, and another person (the checker) reviewing and verifying the statement and the subsequent clearance of the identified reconciling items.

Oct/Nov 2005

18. Which of the following items requires special attention during the reconciliation of a bank's account with the RBI?
(A) Old outstanding balances remaining unadjusted for a significant period.
(B) Standard salary credits to employee accounts.
(C) Fully matched RTGS transactions from the previous day.
(D) Daily interest accruals on standard loan accounts.

Ans :

(A) Old outstanding balances remaining unadjusted for a significant period.
During the reconciliation of accounts with the RBI, special attention must be given to certain types of entries. These include cash transactions that remain unresponded, revenue items that need adjustment or write-off, and particularly, old outstanding balances that have not been adjusted or cleared for a significant period, as these may indicate errors or other issues.

May/June 2023

19. As per RBI mandate, how often should investment balances as per a bank's books be reconciled with the balances in the Public Debt Office's (PDO) books?
(A) Annually
(B) Semi-annually
(C) At quarterly intervals
(D) On a daily basis

Ans :

(C) At quarterly intervals
The RBI has mandated that banks must reconcile their investment balances, specifically for securities, with the records held by the custodian. For balances held in the Public Debt Office's (PDO) books, this reconciliation must be performed at quarterly intervals. If transaction volumes are high, the reconciliation should be conducted more frequently, such as on a monthly basis.

Oct/Nov 2014

20. When reconciling accounts with other banks (other than RBI), what should be ensured regarding bills collected?
(A) That all items which ought to have been taken to revenue for the year have been so taken.
(B) That commission is charged separately and not netted off from the proceeds.
(C) That the net amount is credited immediately, regardless of when commission is booked.
(D) That a provisional credit is given to the customer on the same day the bill is sent for collection.

Ans :

(A) That all items which ought to have been taken to revenue for the year have been so taken.
When reconciling balances with other banks, particular attention is needed for revenue items. It is crucial to ensure that all income that should have been recognized during the year, such as commission on bills collected, has been properly accounted for. This is especially important when net amounts are credited, and commission entries are not made separately.

May/June 2013

21. According to the prevalent practice among banks, how should cheques returned unpaid from clearing be accounted for?
(A) They should be held in a suspense account for seven days.
(B) They should be re-presented in the next clearing cycle without any accounting entry.
(C) They should be ignored in the reconciliation statement until the customer is contacted.
(D) They should be accounted for on the same day or the following day they were sent in clearing.

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vouchers.
II. Pay-in-slips are credit vouchers.
III. Composite vouchers record both debit and credit particulars.
IV. Letters of authority with standing instructions are credit vouchers.
Which of the statements are correct?
(A) I, II, and III only
(B) I, III, and IV only
(C) II, III, and IV only
(D) I, II, and IV only

Ans :

(A) I, II, and III only
Statements I, II, and III are all correct descriptions of different voucher types and their functions. Statement IV is incorrect; a letter of authority with standing instructions to make payments from an account is a form of debit voucher, as it authorizes debits, not credits.

May/June 2023

122. Match List-I (Action) with List-II (Primary Accounting Impact).
List-I (Action)
P. Bank receives cash from a depositor.
Q. Bank pays a cheque issued by a depositor.
R. Bank provides a loan to a borrower.
S. Bank receives a loan repayment installment.
List-II (Primary Accounting Impact)
1. A loan asset decreases.
2. A loan asset is created/increases.
3. A deposit liability increases.
4. A deposit liability decreases.
(A) P-4, Q-3, R-1, S-2
(B) P-3, Q-4, R-2, S-1
(C) P-3, Q-1, R-4, S-2
(D) P-2, Q-4, R-1, S-3

Ans :

(B) P-3, Q-4, R-2, S-1
P: A cash deposit increases the bank's liability to the depositor. Q: Paying a customer's cheque decreases the liability to that depositor. R: Disbursing a loan creates a new asset (loan receivable) for the bank. S: Receiving a repayment installment reduces the outstanding balance of the loan asset.

Oct/Nov 2006

123. The final totals of the day book are entered into the:
(A) Individual subsidiary ledgers.
(B) Cashier's scroll.
(C) Branch manager's report.
(D) Control account in the General Ledger.

Ans :

(D) Control account in the General Ledger.
The day book acts as an intermediary summarization tool. After transactions are posted to individual accounts and summarized in the day book for a particular ledger type (like Savings Bank), the final debit and credit totals from the day book are posted to the corresponding master control account in the General Ledger.

May/June 2016

124. A debit advice received from another branch for a realised collection instrument serves as a debit voucher for which account in the books of the receiving (home) branch?
(A) The customer's account.
(B) The inter-office account.
(C) The cash account.
(D) The commission income account.

Ans :

(B) The inter-office account.
When another branch collects an instrument on your behalf, it credits your branch's account in its books and sends a debit advice. For your branch, this means your claim on that branch has been settled. You will debit the inter-office account (representing the other branch) and credit your customer's account with the proceeds.

Oct/Nov 2020

125. Which statement is INCORRECT regarding transactions in a bank?
(A) Transactions can be broadly classified into cash and non-cash.
(B) Non-cash transactions are also called transfer transactions.
(C) A transfer transaction can only affect two customer accounts.
(D) Payment of interest on deposits is a transfer transaction affecting an internal account.

Ans :

(C) A transfer transaction can only affect two customer accounts.
This statement is too restrictive and therefore incorrect. A transfer transaction can affect two customer accounts (e.g., an internal transfer) or it can affect one customer account and one internal

NODIA

(B) Another credit of ₹5,000 to a control account.
(C) A debit of less than ₹5,000 to an expense account.
(D) One or more debits totaling ₹5,000 to other accounts.

Ans :

(D) One or more debits totaling ₹5,000 to other accounts.
The double-entry system requires that for every credit, there must be an equal and corresponding debit. This can be a single debit to one account or multiple debits to several accounts, as long as the total sum of the debits is equal to the total sum of the credits for the transaction.

Oct/Nov 2025

117. Which of the following is the best example of a debit voucher prepared and authorized solely by the bank without any customer-provided instrument?
(A) A cheque issued by a customer.
(B) A withdrawal slip from a savings account.
(C) An internal voucher for debiting monthly service charges as per terms and conditions.
(D) A letter of authority from a customer.

Ans :

(C) An internal voucher for debiting monthly service charges as per terms and conditions.
Monthly service charges are levied by the bank based on the agreed-upon terms of service. The bank itself generates and authorizes an internal debit voucher to debit the customer's account for these charges. This action doesn't rely on a fresh instrument from the customer for each debit, unlike a cheque or withdrawal slip.

May/June 2007

118. In the context of Mr. A's transactions, which two transactions resulted in a debit to his account?
(A) Cash deposit and Transfer deposit.
(B) Cheque issued to Mr. C (clearing-out) and Draft purchase.
(C) Clearing payment received and Draft purchase.
(D) Cash deposit and Cheque issued to Mr. C.

Ans :

(B) Cheque issued to Mr. C (clearing-out) and Draft purchase.
A debit reduces the account balance. The cheque issued to Mr. C, when paid through clearing, resulted in a debit of ₹4,000. The purchase of the draft for ₹6,000 was also paid for by debiting his account. The other transactions listed were credits, which increased his account balance.

Oct/Nov 2015

119. A key difference between bank accounting and accounting in other enterprises lies in the emphasis and timing of updating which records?
(A) The General Ledger.
(B) The books of prime entry (journals).
(C) The profit and loss account.
(D) The subsidiary ledgers, especially customer accounts.

Ans :

(D) The subsidiary ledgers, especially customer accounts.
The text highlights that in banks, there is a much stronger and more immediate need for the subsidiary ledgers (containing customer accounts) to be accurate and up-to-date. This leads to the peculiar practice of posting to these ledgers first, unlike in other enterprises where journals are typically written up first.

May/June 2009

120. When a customer signs an application for a term deposit, this document acts as a credit voucher because:
(A) It represents the receipt of funds by the bank, creating a liability.
(B) It increases the bank's assets.
(C) It is an instruction to debit another customer's account.
(D) It is a request for the bank to pay money to a third party.

Ans :

(A) It represents the receipt of funds by the bank, creating a liability.
The application for a term deposit is accompanied by funds from the customer. From the bank's perspective, it is receiving money, which increases its cash or is debited from the customer's operative account. The corresponding entry is a credit to a new Term Deposit liability account, making the application a credit voucher.

Oct/Nov 2022

121. Consider the following statements about vouchers:
I. Cheques issued by customers are debit

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and the final step is taking the total from the day book and posting it to the concerned control account within the General Ledger. This completes the cycle of recording from individual transaction to the master ledger.

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bank account (e.g., payment of interest, purchase of a draft). The defining feature is the absence of physical cash.

May/June 2022

126. A 'consolidated voucher' is most likely to be used for which of the following?
(A) Rectifying an error where a debit was posted to the wrong account.
(B) Recording the issuance of a single high-value Letter of Credit.
(C) A customer withdrawing cash using a withdrawal slip.
(D) Crediting half-yearly interest to thousands of savings bank account holders.

Ans :

(D) Crediting half-yearly interest to thousands of savings bank account holders.
A consolidated voucher is specifically designed for efficiency in processing a large number of similar transactions. Crediting interest to thousands of accounts is the perfect use case, where a single voucher for the total amount, supported by a detailed list of individual credits, is prepared instead of thousands of separate vouchers.

Oct/Nov 2012

127. In the illustration, what is the net impact of all transactions on February 28 on Mr. A's account balance?
(A) The balance remained unchanged.
(B) The balance increased by ₹9,000.
(C) The balance decreased by ₹1,000.
(D) The balance decreased by ₹9,000.

Ans :

(A) The balance remained unchanged.
The total credits to Mr. A's account were ₹2,000 (cash) + ₹5,000 (transfer) + ₹3,000 (clearing) = ₹10,000. The total debits were ₹4,000 (clearing) + ₹6,000 (draft) = ₹10,000. Since total credits equal total debits, the net impact on the balance is zero. The closing balance equals the opening balance.

May/June 2021

128. The system of 'voucher posting' facilitates:
(A) Immediate updating of the General Ledger control accounts.
(B) Immediate updating of individual accounts in subsidiary ledgers.
(C) Bypassing the need for any vouchers in the accounting process.
(D) The preparation of financial statements directly from vouchers.

Ans :

(B) Immediate updating of individual accounts in subsidiary ledgers.
The core principle and advantage of 'voucher posting' is that transaction vouchers are posted "straightaway" to the individual accounts in the subsidiary ledgers. This ensures that customer-level records are updated almost in real-time, which is a critical requirement for banking operations, even before totals are compiled for the General Ledger.

Oct/Nov 2005

129. If a customer cancels a demand draft they had previously purchased and gets a refund, the cancelled draft instrument functions as a debit voucher for which account?
(A) The customer's savings account.
(B) The 'Drafts Payable' account.
(C) The bank's commission account.
(D) The cash account.

Ans :

(B) The 'Drafts Payable' account.
When the draft was issued, the bank credited a liability account, 'Drafts Payable'. When the draft is cancelled, this liability is extinguished. To record this, the 'Drafts Payable' account must be debited. The customer's account is credited with the refund. The cancelled instrument authorizes the debit to the liability account.

May/June 2008

130. What is the final step mentioned in the manual accounting process after entries are made in the journal (day book)?
(A) The total is entered in the control account of the General Ledger.
(B) The entries are re-checked by the customer.
(C) The physical vouchers are sent to the head office for archiving.
(D) The individual ledger accounts are updated with the journal entries.

Ans :

(A) The total is entered in the control account of the General Ledger.
The described process flow is: posting to physical ledgers, summarizing in the journal (day book),

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Ans :

(D) To control confirmations and settlement transactions, directly supporting the trading room.

In specialised areas such as Treasury operations and Forex, the back office plays a critical, mainstream role. It directly supports the front office or trading room by managing and controlling essential processes like the confirmation of trades and the settlement of transactions, ensuring operational integrity and control over these high-value activities.

May/June 2009

5. Which of the following activities falls under the 'Book keeping and accounting' function of a bank's back office?

(A) Calculation and posting of interest on various types of customer deposit accounts.
(B) Identifying KYC documentation gaps and managing the customer grievance redressal system.
(C) Reconciliation of entries and sub-systems, and preparation of financial statements.
(D) Processing end-to-end loan originations, including documentation and initial disbursal.

Ans :

(C) Reconciliation of entries and sub-systems, and preparation of financial statements.

The back office's book keeping and accounting functions encompass a range of crucial tasks. These include transaction processing, maintaining the General Ledger, balancing branch accounts, and importantly, the reconciliation of various entries and sub-systems. This group of functions also includes the final preparation of the bank's financial statements, ensuring accuracy and compliance.

Oct/Nov 2017

6. Which back office function group includes tasks like calculation of EMIs, processing fees, and management of operational limits?

(A) Deposits
(B) Loans
(C) e-banking
(D) Regulatory Compliance

Ans :

(B) Loans

The 'Loans' function group within the back office is comprehensive, covering the entire lifecycle of a loan. It includes processing originations, servicing, default management, and collections. It also handles the calculation of EMIs, interest, penal interest, processing fees, and prepayment charges, as well as managing operational limits and risk related to credit products.

May/June 2025

7. Identifying KYC gaps and managing the customer grievance redressal system are responsibilities of which back office function?

(A) Other functions
(B) Book keeping and accounting
(C) e-banking
(D) Regulatory Compliance

Ans :

(D) Regulatory Compliance

The 'Regulatory Compliance' function of the back office is vital for ensuring the bank adheres to legal and regulatory mandates. Key responsibilities under this function include systematically identifying gaps in Know Your Customer (KYC) documentation and managing the customer grievance redressal system, which is a critical aspect of customer service and compliance.

Oct/Nov 2011

8. The handling of transactions through internet, mobile banking, or ATMs falls under which category of back office functions?

(A) e-banking
(B) Deposits
(C) Loans
(D) Clearing and remittances

Ans :

(A) e-banking

The 'e-banking' function of the back office is responsible for managing transactions that occur through various electronic channels. This includes handling payments and other transactions conducted via the internet, mobile banking platforms, Automated Teller Machines (ATMs), and other card-based payment systems, ensuring these transactions are processed correctly and securely.

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CHAPTER 10

Back Office Functions/ Handling Unreconciled Entries in Banks

May/June 2020

1. What is the primary characteristic of back office personnel in a financial services company?

(A) They are primarily involved in sales and marketing activities.

(B) They consist of administration and support personnel who are not client-facing.

(C) They are directly client-facing and manage customer relationships.

(D) They are exclusively located in the main branch of the bank.

Ans :

(B) They consist of administration and support personnel who are not client-facing.

The back office is defined as comprising administration and support personnel within a financial services company who do not have direct interaction with clients. Their functions are crucial for supporting the front office but they operate behind the scenes. Their contribution, while not in the limelight, is major to the overall banking business.

Oct/Nov 2006

2. How has computerisation impacted the division of roles between the front office and back office in banks?

(A) It has resulted in many activities previously done by the front office being moved to the back office.

(B) It has shifted all back office functions to the front office to improve customer service.

(C) It has eliminated the need for a back office by automating all support functions.

(D) It has mandated that front office and back office staff must be co-located in the same branch.

Ans :

(A) It has resulted in many activities previously done by the front office being moved to the back office.

The introduction of computerisation has led to a significant change in roles. Many activities that were once the responsibility of the front office are now performed by the back office. This shift has resulted in cost savings and economies of scale, allowing front office staff to concentrate more on sales and customer servicing functions.

May/June 2014

3. What is a key advantage for banks in locating back offices in different areas or countries?

(A) Proximity to regulatory bodies like the RBI.

(B) Access to a larger client base for business expansion.

(C) Availability of cheaper rents and lower labor costs.

(D) Enhanced visibility and brand recognition in new markets.

Ans :

(C) Availability of cheaper rents and lower labor costs.

Computerisation has removed the necessity for the back office to be part of a specific branch. Consequently, many banks choose to locate their back offices in areas and even other countries where operational costs, particularly rent and labor, are significantly lower. This strategy helps in achieving cost efficiencies and economies of scale for the bank.

Oct/Nov 2023

4. In specialised functions like Treasury and Forex, what is the mainstream role of the back office?

(A) To directly engage in trading activities on behalf of the bank.

(B) To set the foreign exchange rates and treasury investment policies.

(C) To provide financial advice to corporate clients on forex and treasury products.

(D) To control confirmations and settlement transactions, directly supporting the trading room.

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vendor.

(B) The balance of cash in the ATM as per the bank's own books of account.

(C) The balance of cash as recorded by the ATM machine's internal system.

(D) The total amount deposited by customers at the ATM during a day.

Ans :

(C) The balance of cash as recorded by the ATM machine's internal system.

When banks use third-party vendors for ATM management, a centralised department monitors the ATM balances. The balance as per the bank's books is reconciled with the balance as per the ATM machine's own records. This latter balance, recorded by the ATM's system, is commonly referred to as the 'Switch balance'. Reconciliation ensures timely adjustments.

Oct/Nov 2022

14. What is a 'Nostro Account'?

(A) An account maintained by a foreign bank with a bank in India.

(B) An internal account used by a bank to track transactions between its own branches.

(C) A special account maintained with the RBI for statutory reserve requirements.

(D) A foreign currency account maintained by a bank at an overseas centre or with a correspondent bank.

Ans :

(D) A foreign currency account maintained by a bank at an overseas centre or with a correspondent bank.

A 'Nostro Account' is a crucial tool for banks involved in foreign exchange transactions. It refers to a foreign currency account that a bank maintains with an overseas branch or a correspondent bank. The term 'Nostro' is derived from Latin, meaning "our," as in "our account with you," signifying the bank's ownership of the funds in that account.

May/June 2021

15. After reconciling a Nostro account, what do the unmatched items represent?

(A) Items that have not been responded to or were responded to differently by either the bank or its agent.

(B) Transactions that have been successfully completed and settled by both parties.

(C) Accrued interest and commission charges that are yet to be booked in the ledger.

(D) Confirmed future transactions that are pending settlement on their respective value date.

Ans :

(A) Items that have not been responded to or were responded to differently by either the bank or its agent.

The purpose of Nostro account reconciliation is to match the bank's internal records with the statements from the correspondent bank. Any items that remain unmatched after this process represent discrepancies. These are entries that have not been responded to or have been recorded differently in the books of the bank versus its agent, requiring further investigation.

Oct/Nov 2015

16. For what purposes do banks typically maintain accounts with the Reserve Bank of India (RBI)?

(A) For managing employee salary accounts and pension funds.

(B) For facilitating transactions related to CRR, Repo, clearing/RTGS, and currency chests.

(C) Exclusively for investing in government securities and treasury bills.

(D) To handle retail customer deposits and withdrawals on a daily basis.

Ans :

(B) For facilitating transactions related to CRR, Repo, clearing/RTGS, and currency chests.

Banks maintain current and other accounts with the RBI to facilitate various critical regulatory and operational transactions. These include managing Cash Reserve Ratio (CRR) requirements, participating in Repo and Reverse Repo operations, settling high-value transactions through RTGS, participating in clearing systems, and managing currency chest operations for cash distribution.

May/June 2008

17. What is the 'maker checker' concept as applied to the reconciliation of bank accounts with the RBI?

(A) A system where one person makes the transaction and another checks the customer's identity.

(B) A process for preparing the reconciliation statement and subsequently clearing reconciling items.

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May/June 2005

9. Which of the following is NOT listed as a basic reconciliation function group in a bank?
(A) Reconciliation of accounts with correspondent banks.
(B) Reconciliation of inter branch/office entries.
(C) Reconciliation of employee payroll and benefits.
(D) Reconciliation of bank accounts with RBI and other banks.

Ans :

(C) Reconciliation of employee payroll and benefits.
The basic reconciliation functions in a bank are grouped into five specific areas. These are: accounts for payments involving intermediaries, accounts with correspondent banks, accounts with RBI and other institutions, intra-branch entries and sub-systems, and inter-branch/office entries. Employee payroll reconciliation, while an internal accounting function, is not listed among these primary groups.

Oct/Nov 2019

10. Which reconciliation function has remained a significant area of concern for banks, even after the advent of computerisation?
(A) Reconciliation of inter branch/office entries.
(B) Reconciliation of accounts with correspondent banks.
(C) Reconciliation of intra branch entries and sub-systems.
(D) Reconciliation of accounts for payments involving intermediaries.

Ans :

(A) Reconciliation of inter branch/office entries.
The reconciliation of inter-office entries has consistently been a challenging area for banks. Despite advancements in technology and the introduction of computerised systems, fully resolving the issues related to these entries has proven difficult. This makes it a persistent area of concern requiring significant attention from the bank's back office and management.

May/June 2012

11. What role do intermediaries like aggregators and payment gateways play in electronic payment transactions?
(A) They directly provide goods and services to the customers.
(B) They are responsible for manufacturing prepaid payment instruments for banks.
(C) They exclusively handle the logistics and delivery of goods for e-commerce transactions.
(D) They act as platforms where customer payments are credited before transfer to merchants.

Ans :

(D) They act as platforms where customer payments are credited before transfer to merchants.
In the ecosystem of electronic payments for goods and services, intermediaries such as aggregators and payment gateway service providers play a crucial role. Customer payments are first credited to the accounts of these intermediaries. They hold the funds temporarily before transferring them to the respective merchants in the final settlement of the transaction.

Oct/Nov 2008

12. Why has the RBI issued guidelines for the operation of accounts involving payment intermediaries?
(A) To encourage more customers to use online shopping platforms.
(B) To safeguard customer interests and ensure timely remittance of funds to merchants.
(C) To set a standard commission rate for all payment aggregators.
(D) To limit the number of intermediaries a bank can partner with.

Ans :

(B) To safeguard customer interests and ensure timely remittance of funds to merchants.
The RBI's guidelines for accounts involving intermediaries are driven by the need to protect the payment system's integrity. Any delay by intermediaries in transferring funds to merchants poses risks to both customers and merchants. The guidelines aim to ensure payments are duly accounted for and remitted without undue delay, thus ensuring a safe and orderly conduct of transactions.

May/June 2017

13. In the context of ATM operations managed by third-party vendors, what is meant by 'Switch balance'?
(A) The total cash loaded into the ATM by the

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Ans :

(D) They should be accounted for on the same day or the following day they were sent in clearing.
To ensure accurate reconciliation of clearing transactions, there is a standard practice for handling returned cheques. Any cheque that is returned unpaid from the clearing house must be accounted for promptly. Banks are expected to process the return entry on the same day the cheque was originally sent for clearing or, at the latest, on the following day.

Oct/Nov 2021

22. What problem at the branch level has persisted despite the introduction of computerisation in banking?
(A) The balancing of the General Ledger with subsidiary ledgers.
(B) The reconciliation of Suspense and Sundry deposit accounts.
(C) Errors in posting transactions to Savings accounts.
(D) Delays in the totaling of the day book.

Ans :

(B) The reconciliation of Suspense and Sundry deposit accounts.
While computerisation has resolved many historical accounting problems like the balancing of books by automating postings, it has not fully resolved the challenges related to certain accounts. The reconciliation of Suspense accounts and Sundry deposit accounts remains a problem at the branch level that requires manual oversight and timely action to clear outstanding entries.

May/June 2006

23. Under which head of the balance sheet is the balance of a Suspense account typically included?
(A) Capital and Liabilities
(B) Contingent Liabilities
(C) Other Assets
(D) Fixed Assets

Ans :

(C) Other Assets
A Suspense account is used for temporarily recording certain transactions where the final accounting treatment is yet to be determined. If it has a debit balance, which is common for such accounts used to park unclassified debits or losses, it is shown on the assets side of the balance sheet under the head 'other assets'.

Oct/Nov 2013

24. Which of the following is a typical use of a Suspense account in a bank?
(A) To record confirmed profits from the sale of investments.
(B) To hold customer term deposit amounts before maturity.
(C) To account for interest earned on performing loan assets.
(D) To temporarily record amounts until their precise nature is determined.

Ans :

(D) To temporarily record amounts until their precise nature is determined.
The Suspense account serves as a temporary holding account for transactions that cannot be immediately classified. A primary use is to record amounts for which the precise nature has not yet been determined or which are pending transfer to the appropriate head of account. This allows for control over the entry while it is being investigated.

May/June 2011

25. Why does a neglect of control over the Suspense account pose a significant risk?
(A) It can become an easy target for committing frauds by siphoning off funds.
(B) It can lead to an incorrect overstatement of the bank's reported interest income.
(C) It may cause significant operational delays in the renewal of customer term deposits.
(D) It can result in the incorrect calculation and reporting of the Cash Reserve Ratio (CRR).

Ans :

(A) It can become an easy target for committing frauds by siphoning off funds.
A poorly controlled Suspense account is highly susceptible to misuse. Since it is used to hold unclassified debit entries, it can be exploited to commit fraud. Unscrupulous individuals could pass fraudulent debit entries to this account to siphon off money from the bank, making strict control and timely reconciliation of this account critically important.

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sales strategy.
(C) Physically handling cash deposits from customers at the counter.
(D) Calculation and posting of interest for loan accounts.

Ans :

(D) Calculation and posting of interest for loan accounts.
The back office handles various support functions that are not client-facing. The calculation and posting of interest on loan accounts is a core back-office task related to loan servicing. Interacting with clients, approving strategy, and handling cash at the counter are typically front-office or management functions.

Oct/Nov 2014

62. Which of the following is NOT a function typically performed by the back office relating to normal banking activities?
(A) Maintenance of General Ledger and other books of account.
(B) Directly supporting the trading room by executing trades.
(C) Processing end-to-end loan originations.
(D) Handling transactions through internet and mobile banking.

Ans :

(B) Directly supporting the trading room by executing trades.
While the back office in Treasury operations supports the trading room, its role is to control confirmations and settlements, not to execute trades. Executing trades is a front-office function performed by dealers. The other options—maintaining GL, processing loan originations, and handling e-banking transactions—are all standard back-office functions.

May/June 2013

63. Identify the correct statement regarding reconciliation in banks.
(A) Reconciliation of inter-office entries was fully resolved with the advent of computers.
(B) Reconciliation with third-party ATM vendors is not necessary if they are reputable.
(C) The 'maker checker' concept is used for preparing and clearing RBI account reconciliation statements.
(D) Banks are only required to reconcile their accounts with the RBI, not with other banks.

Ans :

(C) The 'maker checker' concept is used for preparing and clearing RBI account reconciliation statements.
The maker-checker concept is a key internal control principle used in preparing the reconciliation statement with the RBI and for the subsequent clearance of reconciling items. Computerisation has not fully resolved inter-office reconciliation, reconciliation with ATM vendors is necessary, and banks must reconcile accounts with RBI and other banks.

Oct/Nov 2021

64. Identify the incorrect statement regarding suspense and sundry accounts.
(A) Suspense account balance is included under 'other assets' in the balance sheet.
(B) Neglect of control over the Suspense account can make it a target for committing frauds.
(C) Losses caused due to frauds awaiting adjustment can be temporarily recorded in a Suspense account.
(D) Sundry Deposits account contains only debit entries and is highly fraud-prone.

Ans :

(D) Sundry Deposits account contains only debit entries and is highly fraud-prone.
This statement is incorrect. The Sundry Deposits account (or Sundries Account) is characterized by credit entries, not debit entries. The Suspense account is the one that typically contains debit entries and is considered more fraud-prone. The other statements about the Suspense account's balance sheet position, fraud risk, and usage are correct.

May/June 2006

65. Match the back office function in List-I with the corresponding activity in List-II.
List-I (Function)
P. Deposits
Q. Loans
R. Regulatory Compliance
S. Book keeping and accounting
List-II (Activity)
1. Identifying KYC gaps
2. Reminders for renewals of term deposits
3. Reconciliation of entries and sub-systems
4. Calculation of EMIs
(A) P-2, Q-4, R-1, S-3

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month.
(C) Only a debit to the customer's account.
(D) An entry in the Nostro account.

Ans :

(A) An Inter Office debit or credit entry.
When a customer uses an ATM of their bank but one that is not linked to their home branch, it constitutes an inter-branch transaction. The customer's account is debited/credited by their home branch, while the branch managing the ATM has a corresponding claim/liability. This is settled through the Inter Office account, creating a debit/credit entry.

May/June 2024

31. Identify the transaction from the list below that results in an Inter Office entry.
(A) Interest calculation on a fixed deposit within a branch.
(B) Payment of electricity bill for the branch premises.
(C) A customer withdrawing cash over the counter at their home branch.
(D) Government receipts handled by a branch as an agent of the nodal branch.

Ans :

(D) Government receipts handled by a branch as an agent of the nodal branch.
When a branch acts as an agent for a nodal branch, for instance, in handling government receipts or payments, it results in inter-office transactions. The collecting branch needs to transfer the funds or account for them with the nodal branch, which necessitates entries through the Inter Office account to track the funds flow between them.

Oct/Nov 2012

32. If the Inter Office account in a branch's books shows a debit balance, where will it appear in that branch's Balance Sheet?
(A) On the liability side under 'Provisions'.
(B) On the assets side.
(C) As a footnote to the Balance Sheet.
(D) On the liability side under 'Deposits'.

Ans :

(B) On the assets side.
A debit balance in the Inter Office account of a branch signifies that this branch has a net claim on other branches or the head office. In accounting, claims on others are assets. Therefore, a debit balance in the Inter Office account is shown on the assets side of that specific branch's Balance Sheet.

May/June 2016

33. For the bank as a whole, where do the net unreconciled inter-office debit adjustments appear in the consolidated Balance Sheet?
(A) Under the head 'Other Liabilities and Provisions'.
(B) Under the head 'Fixed Assets'.
(C) Under the head 'Other Assets'.
(D) They are netted off and do not appear in the Balance Sheet.

Ans :

(C) Under the head 'Other Assets'.
While individual branch transactions should ideally offset each other for the bank as a whole, unreconciled items remain. The net balance of these inter-office adjustments must be shown in the bank's consolidated Balance Sheet. A net debit balance, representing a net claim or un-responded debit, is shown under the head 'Other Assets'.

Oct/Nov 2016

34. What does an unreconciled inter-office entry primarily indicate?
(A) A successfully completed and settled transaction.
(B) A standard time lag that requires no follow-up action.
(C) An increase in the bank's overall profitability.
(D) The existence of errors or, more seriously, frauds.

Ans :

(D) The existence of errors or, more seriously, frauds.
Every inter-office entry should have a corresponding reversal entry from another office. An entry that remains unreconciled after a reasonable period signifies a breakdown in this process. This could be due to a simple error in recording. However, it could also be an indicator of a more serious issue, such as a fraudulent transaction.

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May/June 2022

35. **Assertion (A) :** Every entry in the Inter Office account should be reconciled with a corresponding entry at another branch/office.
Reason (R) : Time lags, such as in the case of drafts issued, are a common and acceptable reason for entries to remain permanently unreconciled.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(C) (A) is true but (R) is false.
Assertion (A) is true; the fundamental principle of inter-office accounting is that every originating entry must be matched by a responding entry. Reason (R) is false because while time lags do cause temporary differences, they are not a reason for entries to remain permanently unreconciled. All entries must eventually be reconciled.

Oct/Nov 2009

36. In a core banking system (CBS), what is the key feature of 'pointing accounts'?
(A) They are used exclusively for high-value transactions.
(B) They require entering a mandatory reference number when passing an entry.
(C) They do not require any reconciliation as they are auto-balanced.
(D) They can only be operated by the branch manager.

Ans :

(B) They require entering a mandatory reference number when passing an entry.
In a CBS environment, office accounts are often bifurcated to streamline reconciliation. 'Pointing accounts' are those that have a mandatory requirement for a unique reference number to be entered with each transaction. This feature makes reconciliation easier as the system can automatically knock off matching entries based on this unique reference number.

May/June 2007

37. Why is reconciliation for 'non-pointing' accounts more difficult than for 'pointing' accounts?
(A) They are used for complex foreign exchange transactions.
(B) The transaction amounts are always in fractions, making them hard to match.
(C) They are not included in the daily statements sent to the reconciliation department.
(D) They involve manual intervention and tracking due to the lack of a unique reference number.

Ans :

(D) They involve manual intervention and tracking due to the lack of a unique reference number.
'Non-pointing' accounts lack the feature of a mandatory unique reference number for each transaction. This absence means that the automated system cannot easily match originating and responding entries. Consequently, reconciliation for these accounts requires manual intervention, tracking, and investigation to identify and clear the outstanding items, making the process more laborious.

NODIA

Oct/Nov 2025

38. Which of the following is listed as a typical error observed in office accounts, though now less common in CBS environments?
(A) Double recording of the same transaction.
(B) Correctly squaring off a transaction after verification.
(C) Posting transactions in the correct office accounts.
(D) Recording particulars in the correct designated fields.

Ans :

(A) Double recording of the same transaction.
Several types of errors were common in manual or older systems. These included recording particulars in incorrect fields, posting to wrong accounts, errors in amounts, and the double recording of a single transaction. While core banking systems have made such errors non-existent or rare, they represent historical challenges in office account reconciliation.

May/June 2015

39. Why does the RBI consider non-reconciliation of inter-office entries a 'fraud risk factor'?
(A) Because it indicates the bank is not using a modern core banking system.
(B) Because it leads to delays in preparing the bank's annual financial statements.
(C) Because unreconciled debit entries can be

used to conceal the siphoning of funds.
(D) Because it increases the operational costs for the bank's back office.

Ans :

(C) Because unreconciled debit entries can be used to conceal the siphoning of funds.
The RBI views non-reconciliation as a significant 'fraud risk factor' due to the potential for misuse. A large number of long-outstanding unreconciled entries, particularly debits, can create an environment where fraudulent transactions are difficult to detect. They can be used to hide the siphoning of funds or to manipulate account statuses, posing a direct financial risk.

Oct/Nov 2018

40. Which of the following is identified by the RBI as an objectionable practice related to office accounts?
(A) Disguising customer cash transactions to avoid reporting requirements.
(B) Using office accounts for their intended purpose of inter-branch settlement.
(C) Making the reference number mandatory for pointing accounts.
(D) Reconciling inter-branch accounts within the stipulated time frame.

Ans :

(A) Disguising customer cash transactions to avoid reporting requirements.
The RBI has observed several objectionable practices by banks involving office accounts. One such practice is using these accounts to disguise large cash transactions of customers. This is done to bypass the system and avoid the mandatory reporting of such transactions, like Cash Transaction Reports (CTRs) or Suspicious Transaction Reports (STRs), to the authorities.

May/June 2010

41. What is the RBI's instruction regarding the timeframe for reconciling outstanding entries in inter-branch accounts?
(A) Within one year.
(B) Within nine months.
(C) Within three months.
(D) Within six months.

Ans :

(D) Within six months.
To ensure timely accounting and mitigate risks associated with long-outstanding entries, the RBI has given clear instructions to banks. It has mandated that banks must reconcile the entries that are outstanding in their inter-branch accounts within a period of six months from the date of the transaction.

Oct/Nov 2007

42. According to RBI guidelines, what should be done with credit entries in inter-branch accounts that are outstanding for more than five years?
(A) They should be written off and charged to the Profit & Loss account.
(B) They should be transferred to a separate Blocked Account.
(C) They should be paid to the government's Depositor Education and Awareness Fund.
(D) They should be netted against debit entries of any age.

Ans :

(B) They should be transferred to a separate Blocked Account.
The RBI has advised banks to segregate very old outstanding credit entries. Any credit entry in inter-branch accounts that remains outstanding for more than five years must be transferred to a separate 'Blocked Account'. This account is then shown in the balance sheet under 'Other liabilities and provisions-Others' (Schedule 5).

NODIA

May/June 2025

43. When calculating the net amount of inter-branch transactions for the balance sheet, how is the 'Blocked Account' treated?
(A) It is added to the total debit entries before netting.
(B) It is netted against debit entries older than five years only.
(C) Its aggregate amount is excluded from the netting process.
(D) It is treated as a contingent liability and shown separately.

Ans :

(C) Its aggregate amount is excluded from the netting process.
The 'Blocked Account', which holds credit entries outstanding for more than five years, receives special treatment in the netting process. The RBI has specified that while arriving at the net amount of inter-branch transactions for

balance sheet purposes, the aggregate amount of the Blocked Account must be excluded. Only the remaining credit entries are netted against debit entries.

Oct/Nov 2019

44. What authorization is required for any adjustment from the 'Blocked Account'?

(A) Authorization by a single branch official.
(B) Authorization by the customer whose transaction is involved.
(C) Authorization from the Reserve Bank of India.
(D) Authorization of two officials, one of whom should be from outside the branch.

Ans :

(D) Authorization of two officials, one of whom should be from outside the branch.
To ensure strong control over the high-risk 'Blocked Account', adjustments are subject to stringent authorization requirements. Any adjustment from this account must be permitted only with the authorization of two officials. If the amount is significant, one of these officials must be from outside the concerned branch, preferably from the controlling or head office.

May/June 2014

45. What was the purpose of the RBI's advice to maintain category-wise (head-wise) accounts for inter-branch transactions starting from April 1, 1999?

(A) To ensure that netting of entries is done on a category-wise basis.
(B) To simplify the process of calculating interest on outstanding balances.
(C) To identify which transaction types are most profitable for the bank.
(D) To automate the entire reconciliation process without manual intervention.

Ans :

(A) To ensure that netting of entries is done on a category-wise basis.
The RBI instructed banks to maintain category-wise or head-wise accounts for inter-branch transactions to bring more discipline to the reconciliation and provisioning process. This segregation allows for netting to be done within specific categories (e.g., drafts payable), preventing banks from offsetting a net debit in one high-risk category with a net credit in another.

Oct/Nov 2006

46. According to the RBI circular DBOD.No.BP. BC.73/21.04.018/2002-03, what provision must be made for unreconciled inter-branch entries?

(A) 50% provision against the gross credit balance in specific categories for entries outstanding over 3 months.
(B) 100% provision against the aggregate net debit balance in all categories for entries outstanding over 6 months.
(C) 20% provision against the gross debit balance across all categories for entries outstanding over one year.
(D) 10% provision against the total unreconciled entries, both debit and credit, as of the balance sheet date.

Ans :

(B) 100% provision against the aggregate net debit balance in all categories for entries outstanding over 6 months.
The RBI circular dated February 26, 2003, mandates a strict provisioning norm for old unreconciled entries. Banks are required to make a provision equivalent to 100 percent of the aggregate net debit balance under all categories for entries that are outstanding in the inter-branch accounts for more than six months as of March 31.

May/June 2007

47. When making the 100% provision for net debit balances, what is the rule regarding set-off between categories?

(A) The net debit in one category can be set-off against the net credit in any other category.
(B) The net debit in one category is not to be set-off against a net credit in another category.
(C) Set-off is permitted only between 'Drafts Payable' and 'Inter-branch Remittances' categories.
(D) All debits and credits across all categories are first aggregated, and provision is made on the final net debit.

Ans :

(B) The net debit in one category is not to be set-off against a net credit in another category.
A crucial part of the provisioning guideline is the prohibition of cross-category netting.

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When calculating the amount for provisioning, banks must ensure that a net debit balance in one category (e.g., government transactions) is not offset or reduced by a net credit balance in another category (e.g., remittances). Provision must be made on the net debit of each category.

Oct/Nov 2017

48. What specific action did RBI advise banks to take regarding the large volume of transactions related to demand drafts?

(A) To segregate these transactions for reconciliation at weekly intervals.
(B) To discontinue the issuance of demand drafts entirely.
(C) To charge a higher commission on all demand draft transactions.
(D) To reconcile demand draft transactions only on an annual basis.

Ans :

(A) To segregate these transactions for reconciliation at weekly intervals.
Recognizing the high volume and inherent risks in demand draft transactions, the RBI issued specific advice for their handling. It directed banks to segregate inter-branch transactions related to demand drafts from other transactions and to establish a system for their reconciliation at more frequent, weekly intervals, along with close monitoring of large amounts.

May/June 2020

49. RBI has advised banks to restrict originating debits to the head office account for certain types of transactions. Which of the following is one such permitted transaction?

(A) Payment of salary to branch staff.
(B) Disbursal of a personal loan to a customer.
(C) Purchase of securities or capital assets.
(D) Payment of rent for the branch premises.

Ans :

(C) Purchase of securities or capital assets.
To improve control over the head office account, RBI has advised banks to restrict the types of transactions for which branches can originate debits. Permitted transactions include essential and controlled activities like cash/funds transfers, purchase of securities/capital assets, withdrawals from the Provident Fund, and advances to inspection and other staff members. Routine operational expenses are generally not included.

Oct/Nov 2011

50. Where is the reconciliation work of Inter Office accounts normally centralised in a modern CBS environment?

(A) At the IT department at the Head Office.
(B) At the largest branch in each city.
(C) At a designated regional office for each zone.
(D) It is decentralised and performed by each branch individually.

Ans :

(A) At the IT department at the Head Office.
In the contemporary Core Banking Solution (CBS) environment, the reconciliation of Inter Office accounts is a highly centralised function. Most banks have centralised this work at their IT department, which is typically located at the Head Office. This allows for automated matching of entries from across the bank's network using centralised data.

May/June 2018

51. If a branch has no Inter Office transactions on a particular day, what must it send to the Central Reconciliation Department (CRD)?

(A) A statement showing the previous day's closing balance.
(B) No statement is required for that day.
(C) An email confirming there were no transactions.
(D) A NIL statement.

Ans :

(D) A NIL statement.
The process requires consistent daily reporting from all branches to the Central Reconciliation Department (CRD). Each branch must send a daily statement of its Inter Office account. To ensure complete reporting and control, if a branch has had no transactions in this account for the day, it is still required to submit a NIL statement.

NODIA

Oct/Nov 2024

52. Which of the following is NOT a reason for an entry remaining unreconciled in the inter-office account system?

(A) A time lag involved in transactions like draft issuance and payment.
(B) A successfully matched originating and responding entry.
(C) A mistake made by a branch in its daily statement.

(D) A fraudulent transaction, such as the payment of a forged draft.

Ans :

(B) A successfully matched originating and responding entry.
The system generates a report of unreconciled entries, which are items that could not be matched. The reasons for an entry being on this list include inherent time lags, mistakes in the data submitted by branches, or fraudulent activities. A successfully matched entry, by definition, is reconciled and would not appear on this report.

May/June 2005

53. What begins where the role of artificial intelligence (the computer system) stops in the reconciliation process?
(A) The automatic generation of the bank's final financial statements.
(B) The role of human intelligence to examine and inquire into unreconciled entries.
(C) The process of initial data entry performed by the individual branches.
(D) The automatic escalation of critical unresolved issues directly to the RBI.

Ans :

(B) The role of human intelligence to examine and inquire into unreconciled entries.
The computer system (or artificial intelligence) is capable of matching entries and generating reports of unreconciled items in various formats. However, its role ends there. The crucial subsequent step requires human intelligence. Staff must examine these reports, inquire with branches about the outstanding entries, and take appropriate decisions to resolve them.

Oct/Nov 2005

54. Which of the following is a common error made by branches in their daily statements that can lead to reconciliation issues?
(A) Using the correct branch code number.
(B) Correctly identifying the type of transaction.
(C) Ensuring the opening balance matches the previous day's closing balance.
(D) Recording the same transaction twice.

Ans :

(D) Recording the same transaction twice.
The accuracy of daily statements submitted by branches is fundamental to the reconciliation process. Common errors that disrupt this process include wrong identification of the transaction type, using incorrect branch codes, errors in amounts, and recording the same transaction more than once. Such mistakes will cause entries to appear as unreconciled.

May/June 2008

55. What does the application of A-B-C analysis in the context of inter-office reconciliation typically involve?
(A) Segregating transactions into high-value, bulk, and other vulnerable items for focused attention.
(B) Classifying all entries alphabetically by branch name.
(C) Arranging all unreconciled entries in chronological order.
(D) Analyzing the cost-benefit of the reconciliation department itself.

Ans :

(A) Segregating transactions into high-value, bulk, and other vulnerable items for focused attention.
A-B-C analysis is a prioritization technique. When applied to inter-office reconciliation, it involves categorizing unreconciled entries to focus efforts effectively. This often means segregating items based on risk and value, such as high-value items ('A'), bulk transactions of moderate value ('B'), and other items ('C'), with special focus on items vulnerable to fraud.

Oct/Nov 2022

56. Special emphasis is placed on scrutinizing certain entries as they may indicate irregular payments or frauds. What type of entries are these?
(A) Originating credit entries.
(B) Reversal entries.
(C) Low-value debit entries.
(D) Entries related to staff accounts.

Ans :

(B) Reversal entries.
Among the practices for effective reconciliation, placing special emphasis on reversal entries is crucial. A reversal entry, especially an unexpected one, could indicate an attempt to correct a fraudulent transaction or could be part of a larger fraudulent scheme. Therefore, these entries are

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scrutinized carefully to detect potential irregular payments or frauds.

May/June 2021

57. What procedure should be in place to handle branches that are habitually late in sending their daily statements?

(A) Imposing a monetary penalty on the branch manager.
(B) Temporarily suspending the branch's ability to perform inter-office transactions.
(C) Identifying such branches and advising the controlling office to follow up with them.
(D) Excluding their transactions from the reconciliation process for that period.

Ans :

(C) Identifying such branches and advising the controlling office to follow up with them.
Timely dispatch of daily statements is critical for the central reconciliation process. A recommended procedure is to have a system that identifies branches that are habitually late in their submissions. The Central Reconciliation Department should then advise the respective controlling office of these branches to follow up and ensure timely compliance.

Oct/Nov 2015

58. How can a bank's computerised reconciliation system help ensure the consistency of daily statements from branches?

(A) By containing an instruction to check that the opening balance of a daily statement tallies with the previous statement's closing balance.
(B) By automatically correcting any errors in the amounts entered by the branch.
(C) By preventing branches from submitting statements with any unreconciled entries.
(D) By sending an alert to the CEO if a branch's statement is late.

Ans :

(A) By containing an instruction to check that the opening balance of a daily statement tallies with the previous statement's closing balance.
A well-designed computerised reconciliation program can build in automated checks to improve data integrity. One such check is to verify the continuity of the statements by ensuring that the opening balance reported on the current day's statement matches the closing balance from the previous day's statement, flagging any discrepancy.

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May/June 2012

59. Why do items in the nature of 'cash-in-transit' require special monitoring in inter-office accounts?

(A) Because they are not expected to remain outstanding beyond a very small period.
(B) Because they typically involve very small amounts of money.
(C) Because they are related to foreign currency transactions only.
(D) Because they can only be initiated by the Head Office.

Ans :

(A) Because they are not expected to remain outstanding beyond a very small period.
'Cash-in-transit' refers to cash being moved between branches or to a currency chest. Such items are included in inter-office accounts but should have a very short lifespan. They require special monitoring because if they remain outstanding for more than a reasonable transit period, it could indicate a delay, loss, or misappropriation of cash.

Oct/Nov 2008

60. As desired by the RBI, how often should a review of the inter-office reconciliation status be conducted by the bank's Board of Directors?

(A) Half-yearly or at even shorter intervals.
(B) Monthly.
(C) Quarterly.
(D) Annually.

Ans :

(A) Half-yearly or at even shorter intervals.
To ensure top-level oversight of this critical risk area, the RBI desires that the Board of Directors of the bank formally review the status of inter-office account reconciliation. This review should be conducted on a half-yearly basis, or even more frequently if the situation warrants, to ensure that issues are being addressed effectively.

May/June 2023

61. Which of the following functions is normally performed by a bank's back office?

(A) Interacting directly with clients to open new accounts.
(B) Approving the bank's overall marketing and

Oct/Nov 2020

26. What is the primary difference between entries in a Suspense account and a Sundry Deposits account?

(A) Suspense account entries are for small amounts, while Sundry Deposits are for large amounts.

(B) Suspense account contains only debit entries, while Sundry Deposits contains credit entries.

(C) Suspense account is reconciled daily, while Sundry Deposits is reconciled monthly.

(D) Suspense account is fraud-proof, while Sundry Deposits is fraud-prone.

Ans :

(B) Suspense account contains only debit entries, while Sundry Deposits contains credit entries.

A key distinction lies in the nature of the entries. A Suspense account is typically used to hold debit balances awaiting classification or adjustment, making it inherently more risk-prone. In contrast, a Sundry Deposits account (or Sundries Account) is used to hold various credit balances, and while needing expeditious clearance, it is considered less susceptible to fraud.

May/June 2019

27. When a bank branch issues a demand draft, which two accounts are typically affected in its books?

(A) The customer's account is credited, and the Inter Office account is debited.

(B) The customer's account is debited, and the Inter Office account is credited.

(C) The cash account is debited, and the customer's account is credited.

(D) The Inter Office account is debited, and another Inter Office account is credited.

Ans :

(B) The customer's account is debited, and the Inter Office account is credited.

When a branch issues a demand draft, it receives funds from the customer. To record this, the customer's account is debited. Since the draft is payable by another branch, a liability is created on behalf of the bank as a whole, which is routed through the Inter Office account. Therefore, the Inter Office account is credited.

Oct/Nov 2010

28. How is the payment of a demand draft by the drawee branch recorded in its books?

(A) The Inter Office account is debited, and the payee's account is credited.

(B) The payee's account is debited, and the Inter Office account is credited.

(C) The cash account is credited, and the payee's account is credited.

(D) The Suspense account is debited, and the Inter Office account is credited.

Ans :

(A) The Inter Office account is debited, and the payee's account is credited.

When the drawee branch pays the demand draft, it credits the account of the payee (or gives cash). To complete the transaction, it needs to record the claim against the issuing branch. This is done by debiting the Inter Office account, which acts as a claim on the branch that originally issued the draft and received the funds.

May/June 2018

29. Which of the following transactions would typically result in an Inter Office debit or credit entry?

(A) A cash deposit made by a customer into their own savings account at their home branch.

(B) The purchase of office stationery for the branch's internal use.

(C) Payment of a draft drawn by another branch of the same bank.

(D) A NEFT transfer initiated by a customer to a beneficiary in another bank.

Ans :

(C) Payment of a draft drawn by another branch of the same bank.

Inter Office entries arise from transactions between different branches or offices of the same bank. Payment of a draft drawn by another branch is a classic example, as the paying branch debits the Inter Office account to claim the funds from the issuing branch. A cash deposit at the home branch is an intra-branch transaction.

Oct/Nov 2024

30. An ATM transaction by a customer at an ATM linked with another branch of the same bank will result in:

(A) An Inter Office debit or credit entry.

(B) No accounting entry until the end of the

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(B) P-4, Q-2, R-3, S-1
(C) P-2, Q-1, R-4, S-3
(D) P-3, Q-4, R-1, S-2

Ans :

(A) P-2, Q-4, R-1, S-3
The correct matching is as follows: The 'Deposits' function includes sending reminders for renewals. The 'Loans' function involves the calculation of EMIs. 'Regulatory Compliance' is responsible for identifying KYC gaps. Finally, 'Book keeping and accounting' includes the crucial task of reconciliation of entries and sub-systems.

Oct/Nov 2013

66. Consider the following statements about inter-office transactions:
1. When a draft is issued, the Inter office account is credited at the issuing branch.
2. When the draft is paid, the Inter office account is debited at the paying branch.
3. If the Inter Office account has a credit balance, it appears on the assets side of the branch balance sheet.

Which of the above statements is/are correct?
(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 only
(D) 1, 2 and 3

Ans :

(A) 1 and 2 only
Statement 1 is correct: the issuing branch receives funds and credits the Inter Office account. Statement 2 is correct: the paying branch pays out funds and debits the Inter Office account to claim them back. Statement 3 is incorrect: a credit balance signifies a liability (the branch owes money to other offices), so it appears on the liability side.

May/June 2011

67. Consider the following statements regarding RBI guidelines on inter-office accounts:
1. Banks must reconcile entries outstanding in inter-branch accounts within a period of six months.
2. Credit entries outstanding for more than three years must be transferred to a Blocked Account.
3. 100% provision is required for the net debit balance on entries outstanding for more than six months.

Which of the statements given above are correct?
(A) 1 and 2 only
(B) 1 and 3 only
(C) 2 and 3 only
(D) 1, 2 and 3

Ans :

(B) 1 and 3 only
Statement 1 is correct, as RBI mandates a six-month reconciliation period. Statement 3 is also correct, as a 100% provision is required for net debit balances outstanding over six months. Statement 2 is incorrect; the period for transferring outstanding credit entries to the Blocked Account is more than five years, not three years.

Oct/Nov 2020

68. Which of the following is NOT one of the major types of transactions that result in an Inter Office debit or credit entry?
(A) Issuance of a locker to a customer at the branch.
(B) Transactions through NEFT, ECS, and RTGS.
(C) Profit/loss transferred by the branch to head office.
(D) Deposits and withdrawal of money by branches from a currency chest maintained by another branch.

NODIA

Ans :

(A) Issuance of a locker to a customer at the branch.
Issuing a locker is a fee-based service provided by a branch to its customer and is an intra-branch transaction. It does not involve another branch or office. The other options, such as electronic fund transfers, profit transfers to the head office, and inter-branch currency chest operations, all inherently involve transactions between different offices of the bank.

May/June 2019

69. Which of the following is the most appropriate description of the reconciliation process for 'pointing accounts' in a CBS?
(A) It requires significant manual tracking due to the non-availability of a reference number.
(B) The reconciliation is easier as entries can be automatically knocked off based on a mandatory reference number.
(C) It is only performed on a quarterly basis due

(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is true; RBI has advised banks to segregate DD transactions and reconcile them weekly. Reason (R) provides the correct justification for this advice. Due to the high volume of DDs and the associated risks, including fraud, a more frequent reconciliation and monitoring cycle is necessary compared to other, less risky transaction types.

Oct/Nov 2006

86. What is the primary purpose of reconciling payments made to online shopping websites via payment gateways?
(A) The intermediary charging a high fee from the merchant.
(B) Any delay in the transfer of funds from the intermediary to the merchant.
(C) The customer changing their mind after making the payment.
(D) The goods supplied by the merchant being of poor quality.

Ans :

(B) Any delay in the transfer of funds from the intermediary to the merchant.
In transactions involving intermediaries, customer payments are first held in the intermediary's account. The primary systemic risk is the potential for delay in the subsequent transfer of these funds to the merchant. Such a delay exposes both the customer (who has paid) and the merchant (who has supplied goods/ services) to financial risk.

May/June 2007

87. A bank's centralised department monitors ATM balances by reconciling the balance as per books with the 'Switch balance'. What does this process ensure?
(A) That the ATM machine never runs out of cash.
(B) That the vendor is charging the correct fee for ATM management.
(C) Timely adjustment of reconciliation entries.
(D) That the ATM is located in a high-traffic area.

Ans :

(C) Timely adjustment of reconciliation entries.
The reconciliation between the bank's book balance and the ATM's switch balance is designed to identify any discrepancies in cash. The ultimate goal of this monitoring and reconciliation process is to ensure that any differences found are investigated and that the necessary adjustment entries are passed in a timely manner to correct the bank's records.

Oct/Nov 2017

88. Consider the following functions:
1. Transaction processing
2. Calculation and posting of interest
3. Identifying KYC gaps
4. Handling transactions through mobile banking
5. Clearing and collection

These functions performed by the back office can be grouped under which of the following heads respectively?
(A) Book keeping, Deposits, Regulatory Compliance, e-banking, Other functions
(B) Deposits, Loans, e-banking, Regulatory Compliance, Other functions
(C) Book keeping, Loans, Deposits, e-banking, Regulatory Compliance
(D) Other functions, Deposits, Regulatory Compliance, e-banking, Book keeping

Ans :

(A) Book keeping, Deposits, Regulatory Compliance, e-banking, Other functions
Transaction processing falls under Book keeping. Calculation of interest is a Deposits function. Identifying KYC gaps is part of Regulatory Compliance. Handling mobile banking is an e-banking function. Clearing and collection are grouped under Other functions. This sequence correctly categorizes each activity according to the provided text.

May/June 2020

89. Which of the following statements about the reconciliation of intra-branch entries is correct?
(A) This process has become more complex with computerisation.
(B) The primary unresolved issue is the reconciliation of Suspense and Sundry deposit accounts.
(C) Special teams are still formed by banks to balance the General Ledger.
(D) RBI has mandated that all intra-branch

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practices for managing inter-office reconciliation?
(A) 1 and 3 only
(B) 2, 3 and 4 only
(C) 1, 2 and 3 only
(D) 1, 2, 3 and 4

Ans :

(D) 1, 2, 3 and 4
All four practices listed are recommended for a robust inter-office reconciliation system. A-B-C analysis helps focus efforts, scrutinizing reversals helps detect fraud, checking opening/closing balances ensures data integrity, and Board-level review ensures top management oversight. These practices collectively strengthen the control environment.

Oct/Nov 2016

74. **Assertion (A) :** In a CBS environment, the problem of balancing the general ledger with subsidiary ledgers is largely non-existent.
Reason (R) : An original entry in an account is automatically posted in all the relevant books and ledgers by the computerised system.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is true; computerisation has resolved the historical problem of unbalanced books. Reason (R) correctly explains why this is the case. In a core banking system, a single transaction entry is automatically and simultaneously posted to the customer's account, the subsidiary ledger, and the general ledger control account, eliminating manual posting errors.

May/June 2022

75. Which statement best describes the treatment of unreconciled inter-office credit adjustments in a bank's consolidated Balance Sheet?
(A) They appear under the head 'Other Liabilities and Provisions'.
(B) They appear under the head 'Other Assets'.
(C) They are shown as a deduction from 'Capital'.
(D) They are not shown in the Balance Sheet but are disclosed in the notes to accounts.

Ans :

(A) They appear under the head 'Other Liabilities and Provisions'.
For the bank as a whole, the net balance of unreconciled inter-office transactions must be reflected in the financial statements. A net credit balance signifies that the bank has a net liability in its inter-office accounts (i.e., it owes funds between its offices). This net credit balance is presented under the head 'Other Liabilities and Provisions'.

Oct/Nov 2009

76. Which of the following is NOT an error typically found in branch daily statements for inter-office accounts?
(A) Wrong identification of the type of transaction.
(B) Automatic matching of entries by the CBS system.
(C) Recording of particulars in incorrect fields.
(D) Difference between the closing and opening balances in successive daily statements.

Ans :

(B) Automatic matching of entries by the CBS system.
The automatic matching of entries is the desired outcome of the reconciliation process performed by the central system, not an error made by the branch in its statement. The other options, such as wrong transaction identification, incorrect data entry, and balance mismatches, are all common errors that can occur at the branch level.

May/June 2007

77. A bank's back office performs various functions related to deposits. Which of the following is one such function?
(A) Deciding the interest rates for new term deposit products.
(B) Conducting marketing campaigns for deposit mobilization.
(C) Sending reminders for renewals of term deposits.
(D) Verifying the customer's signature for a high-value cash withdrawal.

Ans :

(C) Sending reminders for renewals of term deposits.

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The back office handles administrative and support tasks. Sending reminders to customers for the renewal of their maturing term deposits is a classic back-office function related to deposit servicing. Deciding interest rates is a treasury/ ALCO function, marketing is a separate vertical, and signature verification at the counter is a front-office task.

Oct/Nov 2025

78. Consider the following statements:
Statement I : A 'Nostro Account' is a foreign currency account maintained by a bank at an overseas centre.
Statement II : Unmatched items in a Nostro account reconciliation represent transactions that have been successfully settled.
(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Statement I is correct and Statement II is incorrect.
(D) Statement I is incorrect and Statement II is correct.

Ans :

(C) Statement I is correct and Statement II is incorrect.
Statement I correctly defines a 'Nostro Account' as a bank's account in a foreign currency held with a correspondent bank abroad ("our account with you"). Statement II is incorrect because unmatched items represent discrepancies or transactions that have not been responded to, which require further investigation, not successfully settled transactions.

May/June 2015

79. RBI has observed certain objectionable practices by banks concerning office accounts. Which one of the following is such a practice?
(A) Conducting timely reconciliation of inter-branch accounts.
(B) Netting off liability-related GLs with debit balances in other GLs to disclose a lower net outstanding amount.
(C) Using a maker-checker concept for preparing reconciliation statements.
(D) Segregating demand draft transactions for weekly reconciliation as advised.

Ans :

(B) Netting off liability-related GLs with debit balances in other GLs to disclose a lower net outstanding amount.
The RBI has identified the practice of inappropriately netting off General Ledger (GL) accounts as objectionable. This involves taking liability-related GLs with credit balances and setting them off against debit balances in other unrelated GLs. The result is the disclosure of a lower, netted outstanding amount in the financials, which can be misleading.

Oct/Nov 2018

80. Match the term in List-I with its most appropriate description in List-II.
List-I (Term)
P. Originating Entry
Q. Responding Entry
R. Blocked Account
S. Switch Balance
List-II (Description)
1. The initial debit/credit in an inter-office transaction.
2. The balance of cash as per the ATM machine's system.
3. The corresponding credit/debit (reversal) at the other branch.
4. Holds inter-branch credit entries outstanding for more than 5 years.
(A) P-1, Q-3, R-4, S-2
(B) P-3, Q-1, R-2, S-4
(C) P-1, Q-3, R-2, S-4
(D) P-3, Q-1, R-4, S-2

Ans :

(A) P-1, Q-3, R-4, S-2
The correct matching is: P-Originating Entry is the initial transaction (1). Q-Responding Entry is the reversal at the other end (3). R-Blocked Account is for credit entries over 5 years old (4). S-Switch Balance is the balance recorded by the ATM machine itself (2).

May/June 2010

81. What is the primary purpose of reconciling a bank's security balance in its own books with the balance in its SGL or Demat account with a custodian?
(A) To calculate the daily interest accrued on the securities.
(B) To determine the market value of the investment portfolio for trading purposes.

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(C) To fulfill the requirement of filing annual tax returns.
(D) To ensure the bank's record of its investment holdings matches the custodian's record.

Ans :

(D) To ensure the bank's record of its investment holdings matches the custodian's record.
The purpose of this reconciliation is to verify ownership and ensure accuracy of records. The bank's internal books should perfectly match the official records held by the custodian (in a Subsidiary General Ledger or Demat account). This periodic reconciliation helps in identifying any discrepancies in the holding of securities due to errors or unauthorized transactions.

Oct/Nov 2007

82. Which of the following is a key aspect to be ensured while reconciling balances with other institutions and banks (other than RBI)?
(A) That all cheques sent for clearing are outstanding for at least a week.
(B) That all bills or outstanding cheques sent for collection as on the closing date have been credited subsequently.
(C) That credit for interest is always debited from the account.
(D) That charges are debited only at the end of the financial year.

Ans :

(B) That all bills or outstanding cheques sent for collection as on the closing date have been credited subsequently.
When reconciling with other banks, it's crucial to follow up on outstanding items. A key check is to ensure that all instruments like bills or cheques that were sent for collection and were outstanding on the closing date have been successfully credited to the account in the subsequent period, confirming their realization.

May/June 2025

83. Consider the following statements about the reconciliation setup in banks:
1. The reconciliation of Inter Office accounts is typically a decentralised function handled by each branch.
2. If a branch has no inter-office transaction, it need not send any statement to the CRD.
3. The computer system automatically resolves all unreconciled entries without human intervention.

Which of the above statements is/are incorrect?
(A) 1 only
(B) 2 and 3 only
(C) 1 and 2 only
(D) 1, 2 and 3

Ans :

(D) 1, 2 and 3
All three statements are incorrect. Reconciliation is a centralised function, not decentralised. A branch must send a NIL statement even if there are no transactions. The computer system only identifies unreconciled entries; human intelligence is required to investigate and resolve them.

Oct/Nov 2019

84. Which of the following would NOT be a valid reason for using a Suspense Account?
(A) To record an amount pending transfer to the appropriate head of account.
(B) To record debit balances from payment of dividend warrants pending reconciliation.
(C) To permanently park a loss from a fraud without any further action.
(D) To record losses caused by frauds that are awaiting adjustment.

Ans :

(C) To permanently park a loss from a fraud without any further action.
A suspense account is meant for temporary recording of items. While losses from frauds awaiting adjustment can be placed there, it is not meant for permanently parking such losses without any follow-up. The purpose is to hold the entry until a final decision on adjustment, write-off, or recovery is taken, not to indefinitely defer it.

May/June 2014

85. **Assertion (A) :** The reconciliation of inter-office entries related to demand drafts is advised to be done weekly.
Reason (R) : Demand draft transactions represent a large volume and are susceptible to fraud, requiring close monitoring.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.

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to its complexity.

(D) It is a process that has been deemed non-existent in modern core banking systems.

Ans :

(B) The reconciliation is easier as entries can be automatically knocked off based on a mandatory reference number.

The key advantage of 'pointing accounts' in a Core Banking System is the mandatory unique reference number associated with each transaction. This allows the reconciliation system to automatically match and knock off the originating and responding entries, making the process significantly easier, faster, and less prone to error compared to non-pointing accounts.

Oct/Nov 2010

70. A bank is required to make a 100% provision on the aggregate net debit balance for inter-branch entries outstanding for more than six months. Which of the following statements is true in this regard?

(A) A net debit in one category is not set-off against a net credit in another category.

(B) A net debit in the 'drafts payable' category can be offset by a net credit in the 'remittances' category.

(C) The credit balance in the 'Blocked Account' is ignored while calculating the provision.

(D) The provision is calculated on the gross debit balance, not the net debit balance.

Ans :

(A) A net debit in one category is not set-off against a net credit in another category.

The RBI guidelines for this provision are very specific. A crucial rule is that netting is only allowed within a single category of transactions. A net debit in one category cannot be reduced by setting it off against a net credit from a different category. This ensures that provisions adequately cover the risk in each specific area.

May/June 2024

71. Identify the incorrect pair from the following options related to back office functions.

(A) e-banking : Handling transactions through ATMs

(B) Deposits : Sending reminders for renewals of term deposits

(C) Book keeping : Preparation of financial statements

(D) Regulatory Compliance : Calculation of EMIs

Ans :

(D) Regulatory Compliance : Calculation of EMIs

The calculation of EMIs is a core activity related to the 'Loans' function, specifically under loan servicing. The 'Regulatory Compliance' function deals with aspects like identifying KYC gaps and managing the customer grievance redressal system. The other pairs correctly match the function with its corresponding activity.

Oct/Nov 2012

72. Which of the following represents a chronological sequence of events in an inter-branch draft transaction?

1. The responding entry is made by the paying branch.
2. The originating entry is made by the issuing branch.
3. The Central Reconciliation Department matches the entries.
4. A customer requests the issuance of a draft.

(A) 4, 2, 1, 3

(B) 4, 1, 2, 3

(C) 2, 4, 1, 3

(D) 1, 2, 3, 4

Ans :

(A) 4, 2, 1, 3

The logical sequence starts with the customer's request for a draft (4). The issuing branch then creates the draft and makes the originating entry (2). Sometime later, the payee presents the draft at another branch, which makes the payment and the responding entry (1). Finally, the Central Reconciliation Department receives data from both branches and matches the entries (3).

May/June 2016

73. Consider the following practices involved in the reconciliation process:

1. Application of A-B-C analysis to prioritize items.
2. Special emphasis on any reversal entries indicating potential frauds.
3. A system to check if the opening balance of a daily statement tallies with the previous closing balance.
4. Review of the reconciliation status by the Board of Directors.

Which of the above are part of the recommended

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entries must be reconciled daily.

Ans :

(B) The primary unresolved issue is the reconciliation of Suspense and Sundry deposit accounts.

While computerisation has largely solved the problem of balancing the books (GL vs subsidiary ledgers) at the branch level, it has not eliminated all reconciliation challenges. The reconciliation of outstanding entries in the Suspense and Sundry deposit accounts remains an issue that requires ongoing manual effort and decision-making to clear the open items.

Oct/Nov 2011

90. If an unreconciled inter-office transaction remains outstanding, how does it impact the bank's overall balance sheet?

(A) It appears as 'inter office adjustments' under 'Other Assets' (if debit) or 'Other Liabilities' (if credit).

(B) It has no impact as inter-office transactions are internal.

(C) It appears as a 'contingent liability'.

(D) It is directly written off from the Profit and Loss account.

Ans :

(A) It appears as 'inter office adjustments' under 'Other Assets' (if debit) or 'Other Liabilities' (if credit).

For the bank as a whole, all inter-office transactions should net to zero. However, unreconciled items result in a net balance. This balance is presented in the consolidated balance sheet as 'inter office adjustments'. A net debit balance is shown under 'Other Assets', and a net credit balance is shown under 'Other Liabilities and Provisions'.

May/June 2018

91. The following source is provided: "The back office functions relating to the normal banking activities can be grouped as under: Book keeping and accounting: transaction processing, maintenance of General Ledger and other books of account, balancing of branch accounts, reconciliation of entries and sub-systems, preparation of financial statements. Loans: processing end-to-end loan originations or any aspect of loan servicing, loan modification, default management and collections, calculation of EMIs, calculation and posting of interest..."

Based on the source provided, which of the following activities is part of the 'Loans' function group and not the 'Book keeping and accounting' group?

(A) Preparation of financial statements.

(B) Reconciliation of entries and sub-systems.

(C) Maintenance of General Ledger.

(D) Default management and collections.

Ans :

(D) Default management and collections.

According to the provided text, default management and collections are explicitly listed under the 'Loans' function group. The other options, including preparation of financial statements, reconciliation of entries, and maintenance of the General Ledger, are all listed as activities belonging to the 'Book keeping and accounting' function group.

Oct/Nov 2024

92. The following source is provided: "Such a foreign currency account, maintained by a bank at an overseas centre, is designated by it as 'Nostro Account' i.e., "Our account with you"."

According to the excerpt, what is the literal meaning implied by the term 'Nostro Account'?

(A) Your account with us.

(B) Our account with you.

(C) Their account with them.

(D) An account with no owner.

Ans :

(B) Our account with you.

The source explicitly defines the term 'Nostro Account' and provides its direct translation or meaning. It states that the designation 'Nostro Account' means "Our account with you," signifying the bank's perspective of owning an account that is held with another entity (the correspondent bank or overseas branch).

May/June 2005

93. The following source is provided: "In case of purchase and sale of security transactions, the banks periodically reconcile the security balance in the banks book vis-à-vis the balance in the custodian account (i.e., Subsidiary General Ledger or Demat account). It may be noted that RBI has also mandated that investment balances as per bank's book should be reconciled

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Oct/Nov 2008

100. The following source is provided: "Each branch has to send a daily statement of Inter Office account to the Central Reconciliation Department(CRD). If there is no transaction in this account, a NIL statement has to be sent by the branch."
Based on the excerpt, what is the requirement for a branch on a day it has no inter-office transactions?
(A) It must send a NIL statement to the CRD.
(B) It can skip sending the statement for that day.
(C) It must send a copy of the previous day's statement.
(D) It must call the CRD to provide a verbal confirmation.

Ans :

(A) It must send a NIL statement to the CRD.
The text describes a mandatory reporting procedure. To ensure complete control and accounting, the process requires a daily submission from every branch without exception. The source explicitly states that if a branch has no inter-office transactions on a given day, it is still obligated to send a NIL statement to the CRD.

May/June 2023

101. A back office manager at a large commercial bank is tasked with reorganizing the department. The manager needs to group various tasks into logical units. One proposed unit is "Loan Management," which will handle all non-customer-facing aspects of the bank's lending portfolio. Based on the typical functions of a back office, which of the following sets of activities would correctly fall under the new "Loan Management" unit?
(A) Calculation of EMIs, identifying KYC gaps, and handling ATM transactions.
(B) Loan modification, default management, and calculation of penal interest.
(C) Processing loan originations, sending term deposit renewal reminders, and handling remittances.
(D) Risk management for credit products, reconciliation of sub-systems, and customer grievance redressal.

Ans :

(B) Loan modification, default management, and calculation of penal interest.
The "Loans" function in a back office covers the entire lifecycle of a loan. Loan modification, default management, and calculating penal interest are all core activities within loan servicing and management. Identifying KYC gaps is compliance, renewal reminders relate to deposits, and reconciliation of sub-systems is a book-keeping function.

Oct/Nov 2014

102. An auditor reviewing a bank's reconciliation process for its account with the RBI notices a large number of entries flagged for "special attention." These entries are several months old and relate to cash transactions and revenue items. What is the most likely reason these specific entries were flagged for "special attention" during the reconciliation process?
(A) They are items like unresponded cash transactions or revenue items needing adjustment/write-off.
(B) They represent routine, matched transactions that confirm the system is working correctly.
(C) They are related to the purchase and sale of securities in the Demat account.
(D) They represent transactions that have already been cleared and closed in the previous audit period.

Ans :

(A) They are items like unresponded cash transactions or revenue items needing adjustment/write-off.
The reconciliation of accounts with the RBI requires special focus on specific types of problematic entries. These include cash transactions that remain unresponded, revenue items requiring adjustments or write-offs, and old outstanding balances. The auditor's findings directly align with this category of high-risk items that need investigation.

May/June 2013

103. A branch manager discovers that an accountant, to hide a cash shortage, passed a debit entry into an account described as a temporary holding account. This entry has remained un-reconciled for over a month. The manager is concerned about the potential for fraud. Which account was most likely misused by the accountant, given its nature and susceptibility to fraudulent debit entries?

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(D) The amount of the forged draft exceeds a predefined transaction limit.

Ans :

(B) It appears as an unreconciled responding entry with no corresponding originating entry.
The excerpt explains that the paying branch (Branch B) will send a responding entry to the CRD. However, since the draft was forged, the supposed issuing branch (Branch A) has no record and thus sends no originating entry. The CRD's system identifies this one-sided entry as unreconciled, which triggers a follow-up that reveals the fraud.

May/June 2021

97. The following source is provided: "Certain objectionable practices observed by RBI in respect of office accounts are as follows: (a) Disguising the cash transactions of customers to avoid and bypassing reporting... (b) Misuse of funds and indulgence in window dressing... (e) Dummy debits to the office account... to prevent the account from becoming NPA."
According to the text, what is one of the objectionable practices involving "dummy debits" that the RBI has observed?
(A) To increase the reported profits of a branch.
(B) To pay for unapproved capital expenditures.
(C) To create a secret reserve for future contingencies.
(D) To prevent a borrower's account from being classified as a Non-Performing Asset (NPA).

Ans :

(D) To prevent a borrower's account from being classified as a Non-Performing Asset (NPA).
The source explicitly mentions under item (e) that an objectionable practice is the use of "Dummy debits to the office account and credit to the borrowers account... to prevent the account from becoming NPA." This manipulates the borrower's account status, making it appear standard when it should be classified as non-performing.

Oct/Nov 2015

98. The following source is provided: "Banks have been advised by RBI to segregate the credit entries outstanding for more than five years in inter-branch accounts and transfer them to a separate Blocked Account which should be shown in the balance sheet under the head 'Other liabilities and provisions-Others' (Schedule 5)."
Based on the RBI advisory, where should a 'Blocked Account' be presented in a bank's balance sheet?
(A) Under the head 'Other liabilities and provisions-Others'.
(B) Under the head 'Contingent Liabilities'.
(C) Under the head 'Capital and Reserves'.
(D) As a deduction from 'Other Assets'.

Ans :

(A) Under the head 'Other liabilities and provisions-Others'.
The provided text is very specific about the accounting treatment for the Blocked Account. It clearly states that this account, containing credit entries outstanding for over five years, "should be shown in the balance sheet under the head 'Other liabilities and provisions-Others' (Schedule 5)."

May/June 2012

99. The following source is provided: "...the Reserve Bank of India vide its circular DBOD.No.BP. BC.73/21.04.018/2002-03... has advised the banks to make provision against the net debit balance in the inter-branch account in respect of entries outstanding for more than six months... make provision equivalent to 100 percent of the aggregate net debit under all categories."
According to the RBI circular cited, what is the required provisioning for specific unreconciled inter-branch entries?
(A) 50% provision on gross debits outstanding for more than six months.
(B) 100% provision on net credits outstanding for more than one year.
(C) 100% provision on the aggregate net debit balance for entries outstanding over six months.
(D) 10% provision on all unreconciled entries regardless of age.

Ans :

(C) 100% provision on the aggregate net debit balance for entries outstanding over six months.
The source clearly outlines the provisioning rule from the specified RBI circular. It requires banks to make a provision that is equivalent to 100 percent of the aggregate net debit balance. This rule applies specifically to entries in the inter-branch account that have remained outstanding for a period of more than six months.

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at quarterly intervals with the balances in the Public Debt Office's books."

Based on the provided text, what has the RBI mandated regarding the reconciliation of investment balances?

(A) Reconciliation with the Public Debt Office's books must be done daily.
(B) Reconciliation is only required for Demat accounts, not SGL accounts.
(C) Reconciliation at quarterly intervals with the Public Debt Office's books.
(D) Reconciliation of security balances is an optional activity for banks.

Ans :

(C) Reconciliation at quarterly intervals with the Public Debt Office's books.

The source clearly states the RBI's mandate on this matter. It specifies that investment balances as per the bank's books must be reconciled with the balances in the Public Debt Office's (PDO) books. The mandated frequency for this reconciliation is at quarterly intervals, with a provision for more frequent reconciliation if transaction volumes are high.

Oct/Nov 2005

94. The following source is provided: "Suspense account is often used to temporarily record certain items like: (a) Amounts temporarily recorded under this head till the precise nature thereof is determined... (b) Debit balances arising from payment of interest warrants/dividend warrants... (c) Losses caused due to frauds and awaiting adjustment."

As per the excerpt, which of the following is an appropriate use of a Suspense account?

(A) To record confirmed annual profits of the bank.
(B) To hold funds from matured fixed deposits.
(C) To account for regular salary payments to employees.
(D) To record losses from frauds that are awaiting a final adjustment decision.

Ans :

(D) To record losses from frauds that are awaiting a final adjustment decision.

The provided text lists specific, appropriate uses for a Suspense account. Among the listed uses is "(c) Losses caused due to frauds and awaiting adjustment." This indicates that it is a valid, temporary measure to park such an amount in the Suspense account until a final adjustment or write-off can be processed.

May/June 2008

95. The following source is provided: "The typical and most common types of errors observed in office accounts are as under: (a) Recording of particulars in incorrect fields. (b) Posting of transactions in incorrect office accounts. (c) Errors in writing the amounts. (d) Double recording of the same transaction..."

According to the source, which of the following is considered a typical and common error in office accounts?

(A) Recording the same transaction more than once.
(B) Reconciling transactions in a timely manner.
(C) Posting transactions in the correct office accounts.
(D) Using the correct amount for a transaction.

Ans :

(A) Recording the same transaction more than once.

The source lists several common types of errors. The chosen option, recording the same transaction more than once, corresponds directly to item "(d) Double recording of the same transaction" from the provided list of typical errors. The other options describe correct actions, not errors.

Oct/Nov 2022

96. The following source is provided: "What happens if branch A has not issued the draft and the draft paid by the branch B is a forged one. In this case, there will not be any entry pertaining to this draft in the daily statement of Branch A, while the daily statement of branch B will contain a responding entry of ₹5,000. The CRD will not be able to match the responding entry and it will appear as an unreconciled entry..."

Based on the illustration, how is a forged draft payment detected by the Central Reconciliation Department (CRD)?

(A) The CRD system identifies the forged signature on the draft.
(B) It appears as an unreconciled responding entry with no corresponding originating entry.
(C) Branch A sends a specific alert to the CRD about a potential forgery.

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(A) The Sundry Deposits Account.
(B) The branch's Profit and Loss Account.
(C) The Suspense Account.
(D) The branch's Inter Office Account.

Ans :

(C) The Suspense Account.
The Suspense account is described as containing debit entries and being used for temporary purposes. Its neglect can make it an easy target for fraud by passing debit entries to siphon off money. The scenario of hiding a shortage with a debit entry perfectly fits the description of misusing the Suspense account.

Oct/Nov 2021

104. Branch P of ABC Bank pays a demand draft of ₹50,000. The draft appears to have been issued by Branch Q of the same bank. However, Branch Q has no record of issuing such a draft. Both branches submit their daily statements to the Central Reconciliation Department (CRD). How will this fraudulent transaction manifest in the CRD's unreconciled entries report?
(A) A matched entry of ₹50,000, as both debit and credit are present in the system.
(B) An originating debit entry from Branch P and a responding credit entry from Branch Q.
(C) An originating credit entry from Branch Q with no corresponding responding debit entry from Branch P.
(D) A responding debit entry from Branch P with no corresponding originating credit entry from Branch Q.

Ans :

(D) A responding debit entry from Branch P with no corresponding originating credit entry from Branch Q.
Branch P, the paying branch, will submit a responding entry (a debit to the Inter Office account). Branch Q, which did not issue the draft, will have no transaction to report, meaning there will be no originating entry (a credit). The CRD will see a one-sided debit entry, which will appear as an unreconciled item, signaling a discrepancy.

May/June 2006

105. A bank is preparing its annual accounts as of March 31, 2023. The reconciliation department identifies a credit entry of ₹1,00,000 in the inter-branch account that originated on July 15, 2017, and has remained unreconciled since. According to RBI guidelines, what is the correct treatment for this specific entry?
(A) It should be transferred to the separate 'Blocked Account'.
(B) It should be netted against any available debit entry in the inter-branch account.
(C) It should be immediately written off to the Profit and Loss Account.
(D) It should be kept in the normal inter-branch account pending further investigation.

Ans :

(A) It should be transferred to the separate 'Blocked Account'.
The RBI has advised that credit entries in inter-branch accounts that are outstanding for more than five years must be handled separately. Since the entry from 2017 is more than five years old as of 2023, it must be segregated from the normal pool and transferred to the 'Blocked Account'.

Oct/Nov 2013

106. As of March 31, a bank's CRD calculates the position of unreconciled entries older than six months. In the 'Drafts Payable' category, there is a net debit of ₹2 crore. In the 'Inter-branch Remittances' category, there is a net credit of ₹1.5 crore. What is the total amount of provision the bank must make for these unreconciled entries as per RBI norms?
(A) ₹0.5 crore
(B) ₹2 crore
(C) ₹3.5 crore
(D) ₹1.5 crore

Ans :

(B) ₹2 crore
RBI guidelines require a 100% provision on the net debit balance in each category for items outstanding over six months. Crucially, a net debit in one category cannot be set off against a net credit in another. Therefore, the bank must make a full 100% provision on the ₹2 crore net debit, ignoring the net credit.

May/June 2011

107. The CRD of a bank generates a report showing that Branch Z has not submitted its daily inter-office statement for the past three consecutive days. The controlling office for Branch Z is the Zonal Office. What is the most appropriate first step for the CRD to take in this situation?
(A) Immediately stop all inter-office transactions

NODIA

CHAPTER 11
Bank Audit & Inspection

Oct/Nov 2025

1. According to the chapter objectives, which of the following is a key area of understanding a student will gain after studying this unit?
(A) The procedure for filing tax returns for banks
(B) The meaning of audit and the significance of bank audit
(C) The process of developing new banking products
(D) The human resource policies for bank employees

Ans :

(B) The meaning of audit and the significance of bank audit
The chapter objectives clearly state that after studying the unit, the reader will have a better understanding of the meaning of audit and its significance, Risk-Based Internal Audit (RBIA), multiple types of bank audits, and the Reserve Bank of India (RBI) guidelines on bank audit. The other options are not listed as objectives in the chapter.

May/June 2016

2. As defined in "An Introduction to Indian Government Accounts and Audit," what is the primary role of an audit?
(A) To serve as an instrument of financial control
(B) To act as an instrument of business development
(C) To function as a tool for marketing and public relations
(D) To operate as a mechanism for employee performance appraisal

Ans :

(A) To serve as an instrument of financial control
The text quotes the Comptroller and Auditor General of India's book, which defines audit as "An instrument of financial control." It acts as a safeguard on behalf of the proprietor against extravagance, carelessness, or fraud, ensuring that accounts are factual and expenditure is incurred with due regularity and propriety, making it a control mechanism.

Oct/Nov 2009

3. What is the term used for the agency employed to conduct an audit?
(A) A proprietor
(B) An agent
(C) An auditor
(D) A servant

Ans :

(C) An auditor
The definition provided in the text explicitly states, "The agency employed for this purpose is called an auditor." This agency is responsible for safeguarding the proprietor's interests by ensuring financial discipline and accurate representation of facts in the accounts. The other options refer to parties whose actions might be subject to the audit process.

May/June 2023

4. Which legislative act in India makes the audit of company accounts compulsory?
(A) The Banking Regulation Act, 1949
(B) The Reserve Bank of India Act, 1934
(C) The Income Tax Act, 1961
(D) The Companies Act, 2013

Ans :

(D) The Companies Act, 2013
The text specifies that in India, the Companies Act makes the audit of company accounts compulsory. It further mentions that Chapter X of the Companies Act, 2013, deals with various aspects related to auditors, including their appointment, removal, eligibility, powers, and duties, underscoring the mandatory nature of audits for companies under this act.

Oct/Nov 2018

5. What fundamental shift occurred in the main objective of an audit with the increase in company size and transaction volume?
(A) From ensuring a true and fair view to

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(A) That reversal entries may indicate the possibility of irregular payments or frauds.
A key practice in reconciliation is to place special emphasis on reversal entries. While they can be for genuine corrections, a high number of such entries, especially large ones, is a red flag. They can be used to conceal fraudulent activity or irregular payments, and thus should be scrutinized with a high degree of suspicion, not just accepted as routine corrections.

May/June 2024

111. Which of the following is NOT a reason for unreconciled entries in inter-office accounts?
(A) The inherent time lag between issuance and payment of a draft.
(B) A mistake in the amount recorded in a branch's daily statement.
(C) The payment of a forged instrument by a branch.
(D) The automatic knocking off of matched entries in a 'pointing' account.

Ans :

(D) The automatic knocking off of matched entries in a 'pointing' account.
The automatic knocking off of matched entries is the successful outcome of the reconciliation process for 'pointing' accounts. It resolves entries, rather than causing them to remain unreconciled. Time lags, mistakes in statements, and fraud are all valid reasons why an entry might appear on an unreconciled items list.

Oct/Nov 2012

112. What is the primary objective of computerising many back office functions?
(A) To increase the number of client-facing staff in branches.
(B) To achieve cost savings and economies of scale.
(C) To eliminate the need for a Central Reconciliation Department.
(D) To ensure all back offices are located within bank branches.

Ans :

(B) To achieve cost savings and economies of scale.
The text states that the introduction of computerisation has resulted in cost savings and economies of scale. This is achieved by centralizing activities, moving them from the higher-cost front office, and enabling the location of back offices in lower-cost areas, all of which contribute to overall efficiency and reduced expenses.

May/June 2016

113. Consider the following statements:
Statement I : A debit balance in a branch's Inter Office account appears on the liability side of its balance sheet.
Statement II : A credit balance in a branch's Inter Office account appears on the liability side of its balance sheet.
(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Statement I is correct and Statement II is incorrect.
(D) Statement I is incorrect and Statement II is correct.

Ans :

(D) Statement I is incorrect and Statement II is correct.
A debit balance represents an asset (a claim on other offices), so it appears on the assets side, making Statement I incorrect. A credit balance represents a liability (the branch owes other offices), so it correctly appears on the liability side, making Statement II correct.

Oct/Nov 2016

114. The reconciliation function in a bank can be divided into several groups. Which group would handle the reconciliation of payments made to online shopping websites via payment gateways?
(A) Reconciliation of accounts with correspondent banks.
(B) Reconciliation of intra branch entries and sub-systems.
(C) Reconciliation of inter branch/office entries.
(D) Reconciliation of accounts for payments involving intermediaries.

Ans :

(D) Reconciliation of accounts for payments involving intermediaries.
Online shopping payments involving payment gateways fall squarely under the category of transactions with intermediaries. These intermediaries (aggregators, gateways) receive customer payments before settling with merchants. The reconciliation of these accounts

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verify the accuracy of its holdings, identify any discrepancies, and ensure the bank has clear title to its assets.

Oct/Nov 2019

124. Consider the following statements about RBI guidelines for inter-office accounts:

1. Adjustments from the 'Blocked Account' require authorization from two officials.
2. Net debit in one category can be set-off against net credit in another for provisioning purposes.
3. The reconciliation of inter-office entries should be reviewed by the Board of Directors half-yearly.

Which of the statements given above is/are correct?

(A) 1 and 3 only
(B) 1 and 2 only
(C) 2 and 3 only
(D) 1, 2 and 3

Ans :

(A) 1 and 3 only
Statement 1 is correct; strong controls are required for the Blocked Account. Statement 2 is incorrect; RBI specifically prohibits setting off debits and credits across different categories. Statement 3 is correct; the review by the Board should be half-yearly or at even shorter intervals.

May/June 2014

125. The use of 'pointing' and 'non-pointing' accounts is a feature that helps manage reconciliation in which environment?

(A) A fully manual accounting system.
(B) A Core Banking System (CBS).
(C) The reconciliation of Nostro accounts only.
(D) The reconciliation of currency chest transactions only.

Ans :

(B) A Core Banking System (CBS).
The bifurcation of office accounts into 'pointing' (with a mandatory reference number) and 'non-pointing' (without one) is a specific feature found in Core Banking Systems. This design choice is made to facilitate automated reconciliation for certain transaction types while acknowledging that others may still require manual handling.

Oct/Nov 2006

126. A bank's back office handles a variety of regulatory compliance tasks. Which of the following is a prime example of such a task?

(A) Calculation of interest on savings accounts.
(B) Managing the customer grievance redressal system.
(C) Processing a remittance transaction for a customer.
(D) Preparing reminders for term deposit renewals.

Ans :

(B) Managing the customer grievance redressal system.
Managing the customer grievance redressal system is a key regulatory and customer service requirement. This function is categorized under 'Regulatory Compliance' in the back office, as it ensures the bank adheres to prescribed norms for handling and resolving customer complaints in a structured and timely manner.

May/June 2007

127. Which of the following best explains why inter-office reconciliation has remained a "concern for the banks" even with computerisation?

(A) Modern computer systems are often unable to process the high daily volume of inter-office transactions.
(B) The process still relies on manual data entry, which is prone to errors, and requires human intelligence to resolve discrepancies.
(C) There are no clear or consistent RBI guidelines on how to perform the electronic reconciliation process.
(D) The initial and ongoing cost of sophisticated reconciliation software is prohibitively high for most commercial banks.

Ans :

(B) The process still relies on manual data entry, which is prone to errors, and requires human intelligence to resolve discrepancies.
While computers automate matching, the data originates from branch entries, which can have errors. More importantly, the system can only identify mismatches (unreconciled entries). The investigation, follow-up with branches, and decision-making to resolve these discrepancies still require significant human involvement and intelligence, making it an ongoing concern.

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for 8 months. The entry is in the 'Cash Transfer' category. What action is the bank required to take at year-end as per RBI norms?

(A) Ignore the entry as it will likely be reconciled soon.
(B) Make a 50% provision, i.e., ₹25,000, against the entry.
(C) Make a 100% provision, i.e., ₹50,000, against the entry (assuming it's a net debit).
(D) Transfer the entry to the 'Blocked Account'.

Ans :

(C) Make a 100% provision, i.e., ₹50,000, against the entry (assuming it's a net debit).
The RBI mandates a 100% provision against the net debit balance in inter-branch accounts for entries outstanding for more than six months. Since this entry is 8 months old, it falls under this rule. The 'Blocked Account' is for credit entries older than five years, not debit entries.

Oct/Nov 2018

120. Which of the following is NOT an example of a back office function related to loans?

(A) Reminders for renewals of term deposits.
(B) Calculation and posting of interest.
(C) Processing end-to-end loan originations.
(D) Default management and collections.

Ans :

(A) Reminders for renewals of term deposits.
Sending reminders for the renewal of term deposits is a function related to the 'Deposits' group. The other three options—calculating interest, processing originations, and default management—are all core activities that fall under the 'Loans' function group within the back office.

May/June 2010

121. The Central Reconciliation Department (CRD) of a bank is primarily responsible for what task?

(A) Setting the interest rates for loans and deposits.
(B) Directly handling customer complaints and grievances.
(C) Conducting the statutory audit of the bank's financial statements.
(D) Matching originating entries with responding entries from daily inter-office statements.

Ans :

(D) Matching originating entries with responding entries from daily inter-office statements.
The CRD is the central hub for inter-office reconciliation. Its main function is to take the daily statements submitted by all branches and use its systems to match the originating entries from one branch with the corresponding responding (reversal) entries from another, thereby identifying the items that remain unreconciled.

Oct/Nov 2007

122. In the context of inter-office reconciliation, what does the term 'originating entry' refer to?

(A) The final entry that closes a transaction.
(B) The first entry passed at the branch where the transaction begins.
(C) An entry that is passed to correct a previous error.
(D) An entry that is generated automatically by the system without manual input.

Ans :

(B) The first entry passed at the branch where the transaction begins.
An inter-office transaction involves at least two offices. The 'originating entry' is the initial accounting entry that is recorded at the branch where the transaction is initiated. For example, when a draft is issued, the credit to the Inter Office account at the issuing branch is the originating entry.

May/June 2025

123. Why is it important for a bank to reconcile its investment balances with the records of the Public Debt Office (PDO)?

(A) To ensure the bank is earning the maximum possible interest on its investments.
(B) To verify that the bank's records of its government security holdings are accurate.
(C) To get approval from the PDO for all future investment decisions.
(D) To calculate the amount of income tax payable on the investment earnings.

Ans :

(B) To verify that the bank's records of its government security holdings are accurate.
The PDO maintains the official record of government securities held by banks in SGL accounts. Reconciling the bank's own books with the PDO's records is a critical control measure to

for Branch Z.

(B) Send a high-level report directly to the bank's Board of Directors.

(C) Advise the Zonal Office to follow up with Branch Z to ensure compliance.

(D) Assume a NIL transaction day and close the books for Branch Z.

Ans :

(C) Advise the Zonal Office to follow up with Branch Z to ensure compliance.

The established procedure for handling habitually late branches involves escalation to their immediate controlling authority. The CRD's role is to identify such branches and inform the controlling office (in this case, the Zonal Office), which is then responsible for following up with the branch and enforcing discipline in submitting the statements.

Oct/Nov 2020

108. An internal auditor reviews a branch's inter-office account and finds several large debit entries to the Head Office account. The narrations mention "customer loan disbursal" and "payment of branch rent." The auditor flags these as irregular. Why would the auditor consider these entries irregular based on RBI guidelines?

(A) Because RBI has advised restricting originating debits to the Head Office account to specific transactions like fund transfers or asset purchases.

(B) Because all debits to the Head Office account must be for amounts less than a small, predefined threshold of ₹10,000.

(C) Because loan disbursals and rent payments must be routed exclusively through the branch Suspense Account.

(D) Because branches are strictly not permitted to have any debit entries in their Head Office account under any circumstances.

Ans :

(A) Because RBI has advised restricting originating debits to the Head Office account to specific transactions like fund transfers or asset purchases.

The RBI has specifically advised banks to restrict the types of transactions for which branches can originate debits to the Head Office account. Routine operational expenses like rent and customer loan disbursals are not on the permitted list, which includes items like cash transfers, security purchases, etc. This makes the entries irregular.

May/June 2019

109. A bank's back office uses a Core Banking System where inter-office accounts for government transactions are set up as 'non-pointing' accounts, while accounts for draft payments are set up as 'pointing' accounts. What is the most significant implication of this setup for the reconciliation process?

(A) Reconciliation of government transactions will be easier than draft payments.

(B) Reconciliation of draft payments will be easier and more automated.

(C) Both account types will require the same level of manual intervention.

(D) The system will be unable to reconcile government transactions at all.

Ans :

(B) Reconciliation of draft payments will be easier and more automated.

'Pointing' accounts use a mandatory reference number, allowing the system to automatically match and knock off entries. 'Non-pointing' accounts lack this feature and require manual tracking. Therefore, the reconciliation for draft payments (pointing) will be significantly easier and more automated than the reconciliation for government transactions (non-pointing).

Oct/Nov 2010

110. A bank's Board of Directors is conducting its half-yearly review of unreconciled inter-office entries. The report shows a large number of outstanding reversal entries from a particular region, which the management claims are for correcting minor data entry errors. What should be the Board's primary concern regarding these reversal entries, based on standard reconciliation practices?

(A) That reversal entries may indicate the possibility of irregular payments or frauds.

(B) That the entries are cluttering the report and should be hidden.

(C) That the staff correcting the errors are not being efficient enough.

(D) That the bank's software is not functioning correctly.

Ans :

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Oct/Nov 2017

128. What is the key difference in risk profile between a Suspense Account and a Sundry Deposits Account?

(A) The Suspense Account is more fraud-prone as it contains debit entries that can hide siphoning of funds.
(B) The Sundry Deposits Account is more fraud-prone as it contains credit entries.
(C) There is no difference in risk; both are equally susceptible to fraud.
(D) The Suspense Account is low-risk as it is reconciled daily, unlike the Sundry Deposits Account.

Ans :

(A) The Suspense Account is more fraud-prone as it contains debit entries that can hide siphoning of funds.
The text explicitly contrasts the two. The Suspense Account, which contains only debit entries, is highlighted as an easy target for fraud by passing debit entries to siphon off money. The Sundry Deposits Account, containing credit entries, is noted to be less fraud-prone, although it still requires expeditious clearing.

May/June 2020

129. A bank's back office in a Tier-II city handles loan processing for all its metropolitan branches. This arrangement is primarily an example of leveraging which advantage of modern back office structures?

(A) Proximity to the trading room for quick settlements.
(B) Focusing front office staff on sales and servicing functions.
(C) Compliance with RBI's mandate for rural banking.
(D) Enhanced brand visibility in the Tier-II city.

Ans :

(B) Focusing front office staff on sales and servicing functions.
By centralizing loan processing in a separate back office, the front office staff in the metropolitan branches are freed from administrative tasks. This allows them to dedicate their time and effort to core, client-facing activities like sales and customer service, thereby improving business performance, which is a key benefit highlighted in the text.

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Oct/Nov 2011

130. A bank is reconciling its account with another bank where it maintains an account for clearing purposes. It notices a debit entry for 'charges' that has not been accounted for in its own books. What is the immediate action required?

(A) To ensure the charge is properly taken to revenue (expense) for the year.
(B) To dispute the charge with the other bank.
(C) To wait for the other bank to reverse the entry.
(D) To move the entry to the Suspense account indefinitely.

Ans :

(A) To ensure the charge is properly taken to revenue (expense) for the year.
When reconciling with other banks, it's crucial to ensure all revenue and expense items are accounted for correctly. The text emphasizes that it should be ensured that no debit for charges is outstanding and that all items that ought to have been taken to revenue for the year have been so taken.

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of judgment and the inability to check every transaction, means an audit provides reasonable, not absolute, assurance.

Oct/Nov 2006

10. What is the primary purpose of a bank audit as described in the text?
(A) To review financial statements, services, and procedures to ensure compliance with laws and RBI guidelines
(B) To increase the bank's profitability and market share
(C) To train bank staff on new accounting principles and practices
(D) To exclusively focus on the detection of employee fraud

Ans :

(A) To review financial statements, services, and procedures to ensure compliance with laws and RBI guidelines
Bank audit is defined as the procedure of reviewing the financial statements, services, and procedures adopted by banks. This review is conducted as required under various legislations and the guidelines of the Reserve Bank of India, ensuring that the bank complies with industry standards and regulatory norms, which is crucial for maintaining stability and public confidence.

May/June 2021

11. Historically, what was the primary focus of the internal audit system in banks before the emergence of RBIA?
(A) Evaluating the effectiveness of risk management procedures
(B) Proactively identifying new and potential business risks
(C) Assessing the governance processes at the corporate level
(D) Transaction testing and checking the accuracy of accounting records

Ans :

(D) Transaction testing and checking the accuracy of accounting records
The text states that the internal audit system in banks historically concentrated on transaction testing. This included testing the accuracy and reliability of accounting records and financial reports, ensuring the integrity of control reports, and verifying adherence to legal and regulatory requirements, which is a more reactive and compliance-focused approach compared to modern risk-based auditing.

Oct/Nov 2010

12. When did the RBI first introduce the Risk-Based Internal Audit (RBIA) system in Scheduled Commercial Banks?
(A) January 07, 2021
(B) December 27, 2002
(C) September 18, 2019
(D) April 29, 2011

Ans :

(B) December 27, 2002
The chapter specifies that the Reserve Bank of India (RBI) introduced the Risk-Based Internal Audit (RBIA) system in Scheduled Commercial Banks (SCBs) as part of their internal control framework vide a circular dated December 27, 2002. This marked a significant shift towards a more proactive and risk-focused approach in bank internal audits.

May/June 2005

13. What is the core principle of Risk-Based Internal Auditing (RBIA)?
(A) It is a system focused exclusively on full-scale transaction testing to find errors
(B) It is a process for auditing risks directly rather than the management of risks
(C) It is a methodology that links internal auditing to an organisation's overall risk management framework
(D) It is a technique to replace internal auditors with external consultants for all audit functions

Ans :

(C) It is a methodology that links internal auditing to an organisation's overall risk management framework
The text defines Risk-Based Internal Auditing as a methodology that links internal auditing to an organisation's overall risk management framework. RBIA allows the internal audit function to provide assurance to the Board and Senior Management on the quality and effectiveness of the bank's internal controls, risk management, and governance systems and processes.

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ensuring arithmetical accuracy
(B) From detecting fraud to preventing extravagance
(C) From ascertaining accounts were true and correct to ensuring they were true and fair
(D) From ascertaining a true and fair representation to ensuring accounts were true and correct

Ans :

(C) From ascertaining accounts were true and correct to ensuring they were true and fair
The text highlights a significant evolution in auditing objectives. Initially focused on arithmetical accuracy ("true and correct"), the emphasis shifted. With growing business complexity, the main goal became to ascertain whether the accounts provided a "true and fair" representation of the financial state of affairs, focusing on fairness over mere numerical correctness.

May/June 2007

6. What does the acronym CAATs stand for in the context of modern auditing?
(A) Computer Aided Accounting Techniques
(B) Computer Aided Audit Techniques
(C) Corporate Accounting and Auditing Tools
(D) Centralized Audit and Analysis Tools

Ans :

(B) Computer Aided Audit Techniques
The chapter introduces CAATs as Computer Aided Audit Techniques. These techniques have become integral to the audit process, especially in a computerized environment. They are used to process data of audit significance and to improve the overall effectiveness and efficiency of the audit, representing a shift from manual checking to technology-driven analysis.

May/June 2012

7. In the context of a Computerised Information System environment, how has the paradigm of audit procedures shifted?
(A) From 'clicks' to 'ticks'
(B) From 'Auditing through the computer' to 'Auditing around the computer'
(C) From financial audit to operational audit
(D) From 'Auditing around the computer' to 'Auditing through the computer'

Ans :

(D) From 'Auditing around the computer' to 'Auditing through the computer'
The text describes a paradigm shift in audit procedures due to computerization. The approach has transformed from 'Auditing around the computer,' which treated the computer as a black box, to 'Auditing through the computer,' which involves using the computer itself to test controls and process data. This is also characterized as a shift from 'ticks' to 'clicks'.

Oct/Nov 2014

8. Which of the following is identified as an incidental objective of auditing?
(A) Detection and prevention of errors and frauds
(B) Expressing an opinion on financial statements
(C) Ensuring compliance with all management policies
(D) Verifying every single transaction of the business

Ans :

(A) Detection and prevention of errors and frauds
While the primary objective of an audit is to express an opinion on the truth and fairness of financial statements, the text mentions that the detection and prevention of errors and frauds are considered incidental objectives. These are important by-products of the main audit process, though not its central aim in modern auditing.

May/June 2019

9. Which of the following is considered an inherent limitation of auditing?
(A) The auditor must check each and every transaction
(B) The auditor's work does not involve the exercise of judgment
(C) The auditor has to depend on explanations provided by others
(D) The audit report guarantees the future viability of the business

Ans :

(C) The auditor has to depend on explanations provided by others
The chapter lists several inherent limitations of auditing. One key limitation is that auditors must often rely on information and explanations provided by the company's management and staff. This dependency, along with the use

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is crucial to ensure funds are transferred correctly and is a distinct function group.

May/June 2022

115. Which of the following is the best description of a 'reversal entry' in the context of inter-office accounts?

(A) A corresponding credit/debit transaction that matches an originating entry.
(B) The first entry made when a transaction is initiated.
(C) An entry made to correct a typing error in a customer's name.
(D) A monthly entry to book interest on the account balance.

Ans :

(A) A corresponding credit/debit transaction that matches an originating entry.
In inter-office accounting, an 'originating entry' (e.g., a credit) at one branch must be matched by a 'responding' or 'reversal' entry (a debit of the same amount) at another branch. This corresponding entry effectively reverses the initial entry on a bank-wide basis, allowing the transaction to be settled and reconciled between the offices.

Oct/Nov 2009

116. A bank's IT department is designing a new reconciliation system. To comply with best practices, what check should be included regarding daily statements?

(A) A check to ensure all transaction amounts are even numbers.
(B) A check to ensure the opening balance matches the previous day's closing balance.
(C) A check to ensure the number of transactions is below 100 per day.
(D) A check to ensure all narrations are written in capital letters.

Ans :

(B) A check to ensure the opening balance matches the previous day's closing balance.
A fundamental check for data integrity and continuity is to verify that the opening balance of a branch's daily statement for any given day is exactly the same as the closing balance reported on the statement from the immediately preceding day. Any mismatch indicates a break or error in the accounting sequence.

May/June 2007

117. What is the fundamental reason that a neglect of control over a Suspense Account is considered a major operational risk?

(A) It can lead to incorrect calculation of interest on deposits.
(B) It can be used to pass debit entries to siphon off funds from the bank.
(C) It complicates the process of reconciling currency chest transactions.
(D) It can cause delays in processing RTGS and NEFT payments.

Ans :

(B) It can be used to pass debit entries to siphon off funds from the bank.
The primary risk of a poorly controlled Suspense Account is its vulnerability to fraud. Because it is used to hold unclassified debits, it provides an opportunity for individuals to conceal fraudulent withdrawals or transfers by parking the corresponding debit entry in this account, making it difficult to detect the siphoning of funds.

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Oct/Nov 2025

118. Which statement accurately reflects the impact of computerisation on branch-level reconciliation?

(A) It has solved the problem of balancing books but not the reconciliation of suspense accounts.
(B) It has completely eliminated the need for any reconciliation at the branch level.
(C) It has made the reconciliation of inter-office entries a simple, error-free process.
(D) It requires branches to form special teams for reconciling savings accounts.

Ans :

(A) It has solved the problem of balancing books but not the reconciliation of suspense accounts.
The text highlights that computerisation has been highly effective in solving the historical problem of balancing the general ledger with subsidiary ledgers. However, it explicitly states that the problem of reconciling Suspense and Sundry deposit accounts, which requires investigation and decision-making, has not been resolved by computerisation alone.

May/June 2015

119. A bank discovers a debit entry of ₹50,000 in its inter-branch account that has been outstanding

Oct/Nov 2022

14. Under Risk-Based Internal Audit, the focus shifts from full-scale transaction testing towards what?
(A) Verifying arithmetical accuracy of all ledger accounts
(B) Checking compliance with human resource policies only
(C) Ensuring the physical security of all bank branches
(D) Risk identification, prioritization of audit areas, and allocation of audit resources

Ans :

(D) Risk identification, prioritization of audit areas, and allocation of audit resources
The text clarifies that under RBIA, the focus moves away from the historical method of comprehensive transaction testing. Instead, the emphasis is on identifying and assessing risks, prioritizing audit areas based on this risk assessment, and then allocating audit resources accordingly to focus on the areas of highest risk within the organization.

May/June 2018

15. What is the primary focus of RBIA, as stated in the chapter?
(A) Auditing the process applied by the management team to respond to risks
(B) Auditing risks themselves
(C) Auditing the financial performance of business lines
(D) Auditing every transaction that occurs at the branch level

Ans :

(A) Auditing the process applied by the management team to respond to risks
The chapter makes a crucial distinction by stating, "RBIA is not about auditing risks but about auditing the management of risk." It emphasizes that the focus of RBIA is on the processes and systems that the management team has implemented to identify, measure, monitor, and control the risks faced by the bank.

Oct/Nov 2016

16. According to RBI instructions, who should the Head of Internal Audit (HIA) be?
(A) A mid-level officer with experience in a single department
(B) A senior executive of the bank with the ability to exercise independent judgement
(C) An external consultant hired on a permanent basis
(D) The head of a major business vertical within the bank

Ans :

(B) A senior executive of the bank with the ability to exercise independent judgement
The RBI instructions on 'Authority, Stature and Independence' mandate that the Head of Internal Audit (HIA) must be a senior executive of the bank. This position requires the individual to have sufficient stature to exercise independent judgement and carry out their responsibilities with objectivity, free from undue influence from the business lines.

May/June 2014

17. What desired areas of knowledge and experience are mentioned for an effective internal audit function?
(A) Only accounting and banking operations
(B) Banking operations, accounting, IT, data analytics, and forensic investigation
(C) Marketing, human resources, and public relations
(D) Only legal compliance and statutory reporting

Ans :

(B) Banking operations, accounting, IT, data analytics, and forensic investigation
The section on 'Competence' highlights that for an internal audit function to be effective, auditors must possess requisite professional competence across several domains. The text explicitly lists banking operations, accounting, information technology, data analytics, and forensic investigation as desired areas of knowledge and experience for internal auditors to comprehensively cover all aspects of the bank.

Oct/Nov 2007

18. What is the RBI's recommendation regarding the tenor for the appointment of the Head of Internal Audit (HIA), except in specialized cases?
(A) A minimum of three years
(B) A minimum of one year
(C) A maximum of two years
(D) A period left entirely to the discretion of the MD & CEO

Ans :

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Oct/Nov 2013

36. Which of these is a key objective that an IS Audit aims to determine if a computer system can achieve?
(A) Maximize the number of daily transactions
(B) Maintain data integrity
(C) Ensure the highest possible employee satisfaction
(D) Generate the maximum number of marketing leads

Ans :

(B) Maintain data integrity
The text lists four main determinations of an IS Audit. One of these is to see if the computer system can "maintain data integrity." This is a critical function, as the reliability of all financial reporting and decision-making depends on the integrity and accuracy of the underlying data processed and stored by the IT systems.

May/June 2015

37. The RBI guidelines on Information Systems Audit issued on 29th April, 2011 cover several areas. Which of the following is NOT one of those areas?
(A) Information Technology (IT) Governance
(B) Business Continuity Planning
(C) Branch location and design
(D) Cyber Fraud

Ans :

(C) Branch location and design
The chapter provides a list of nine areas covered by the RBI's 2011 guidelines on IS Audit. This list includes IT Governance, Information Security, IS Audit, IT Operations, IT Services, Outsourcing, Cyber Fraud, Business Continuity Planning, and Customer Awareness. Branch location and design is a physical infrastructure concern, not an IT governance or security issue.

Oct/Nov 2012

38. According to the scope of an IS Audit, what action should be taken after identifying deficient controls?
(A) Report them directly to the media to ensure public awareness and prompt management action
(B) Ignore them if they are minor and do not have a direct financial impact on the statements
(C) Immediately recommend the replacement of the entire IT system regardless of the cost involved
(D) Recommend corrective action and follow-up to ensure implementation

Ans :

(D) Recommend corrective action and follow-up to ensure implementation
The scope of an IS Audit includes several key activities. The final point listed is "Identifying deficient controls, recommend corrective action to address deficiencies and follow-up and to ensure that the management effectively implements the required actions." This completes the audit loop from identification of a problem to its resolution and verification.

May/June 2011

39. What is a key reason for the IS Audit Function to enhance the use of Computer-Assisted Audit Techniques (CAATs)?
(A) For critical functions or processes carrying financial or regulatory implications
(B) To reduce the number of auditors required
(C) Because manual techniques are no longer permitted by law
(D) To create more complex and difficult audit procedures

Ans :

(A) For critical functions or processes carrying financial or regulatory implications
The text states that the IS Audit Function needs to enhance the use of CAATs, "particularly for critical functions or processes carrying financial or regulatory or legal implications." This is because CAATs can be more efficient and effective than manual techniques for analyzing large volumes of data and testing controls in these high-risk areas.

Oct/Nov 2020

40. Which of the following is a critical area where CAATs may be used?
(A) Monitoring customer transactions under AML requirements
(B) Designing the layout of a new branch
(C) Conducting employee satisfaction surveys
(D) Deciding on the bank's advertising budget

Ans :

(A) Monitoring customer transactions under AML requirements

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(D) By structuring it to avoid linkage to the financial performance of the business lines they audit

The section on 'Remuneration' explains that the independence and objectivity of the internal audit function can be undermined if their pay is tied to the performance of the business units they are responsible for auditing. Therefore, remuneration policies should be structured to avoid creating a conflict of interest, preserving the audit's integrity.

May/June 2010

23. Under what condition can a bank hire external experts, including former employees, for the internal audit function?

(A) Whenever the bank wants to reduce operational costs associated with permanent audit staff

(B) Only if the external experts agree to work on a pro-bono basis to avoid any financial conflict of interest

(C) When the Audit Committee of the Board is assured that such expertise does not exist within the bank

(D) There are no conditions for non-critical areas; outsourcing is freely permitted by the Board

Ans :

(C) When the Audit Committee of the Board is assured that such expertise does not exist within the bank

The guideline on 'Outsourcing' states that the internal audit function itself shall not be outsourced. However, it provides an exception for hiring experts on a contractual basis. This is permissible only when required, and the Audit Committee of the Board (ACB) must be assured that the necessary expertise is not available internally.

Oct/Nov 2024

24. If external experts are hired for an internal audit assignment, who retains the ownership of the audit reports?

(A) The regular functionaries of the internal audit function

(B) The external experts who prepared the report

(C) The Audit Committee of the Board

(D) The Reserve Bank of India

Ans :

(A) The regular functionaries of the internal audit function

The guidelines on outsourcing are clear about accountability. Even when external experts are hired to assist, the text specifies that "Ownership of audit reports in all cases shall rest with regular functionaries of the internal audit function." This ensures that the bank's own audit department remains responsible and accountable for the final audit work and its outcomes.

May/June 2017

25. Into which three broad categories can bank audits be classified?

(A) Financial, Operational, and Compliance Audits

(B) Branch, Head Office, and Zonal Audits

(C) Concurrent, Internal/Information System, and Statutory Audits

(D) Pre-audit, Post-audit, and Continuous Audit

Ans :

(C) Concurrent, Internal/Information System, and Statutory Audits

The chapter explicitly classifies bank audits into three broad categories to address the need for authenticity and reliability of accounts. These categories are listed as 1. Concurrent Audit, 2. Internal Audit/Information System Audit, and 3. Statutory Audit, each serving a distinct purpose in the overall audit framework of a bank.

Oct/Nov 2005

26. What is the defining characteristic of a Concurrent Audit?

(A) It is performed once a year after the books are closed

(B) It is an examination that is contemporaneous with the occurrence of transactions

(C) It is conducted exclusively by the bank's own internal staff

(D) It focuses only on the bank's IT systems and controls

Ans :

(B) An examination that is contemporaneous with the occurrence of transactions

The text defines concurrent audit as an examination which is "contemporaneous with the occurrence of transactions or is carried out as near thereto as possible." Its purpose is to shorten the interval between a transaction and its

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(A) Mandated or compulsorily required by any law or Act

The chapter provides a clear definition under the salient features of a statutory audit. It explains that the word 'Statute' in 'Statutory Auditor' means "mandated or compulsorily required by any law or Act." This highlights that the audit is not optional but a legal obligation imposed by a legislative body.

May/June 2023

46. Which section of the Banking Regulation Act, 1949 requires the audit of a banking company's Balance Sheet and Profit and Loss account?

(A) Section 20(1)
(B) Section 30(1)
(C) Section 49(A)
(D) Section 10(1)

Ans :

(B) Section 30(1)

The text explicitly states under the salient features of statutory audit that "In case of Banks, sub-section (1) of Section 30 of the Banking Regulation Act, 1949 requires that the Balance Sheet and Profit and Loss account of a banking company should be audited." This is the specific legal provision mandating the audit.

Oct/Nov 2018

47. How does a statutory audit's approach to banking transactions differ from that of concurrent and internal audits?

(A) It examines every single transaction in detail
(B) It completely ignores banking transactions and focuses only on governance
(C) It relies on the reports of concurrent and internal audits and uses test checking
(D) It is less independent than internal and concurrent audits

Ans :

(C) It relies on the reports of concurrent and internal audits and uses test checking

The chapter clarifies the difference in scope. It states that a statutory audit "does not look at the intricacies of the banking transactions (which are looked into by concurrent and Internal audits); instead they rely on the concurrent audit & internal Audit Reports and test checking to form their opinion." This shows a higher-level, opinion-based approach.

NODIA

May/June 2007

48. Which of the following areas is a primary focus for a statutory audit?

(A) Employee training programs and satisfaction levels
(B) Marketing campaign effectiveness and brand image
(C) Daily cash management and branch-level operational efficiency
(D) Compliance with CRR, SLR, CRAR, and PSL requirements

Ans :

(D) Compliance with CRR, SLR, CRAR, and PSL requirements

The text specifies the main areas of focus for a statutory audit. It "mainly looks at the loans and advances, Compliance with Priority Sector Lending (PSL) requirements, CRR, SLR, CRAR etc. and other Statutory norms compliance as per latest RBI guidelines." These are key regulatory and systemic aspects of a bank's functioning.

May/June 2012

49. Which of the following is one of the initial stages in a Bank/Statutory audit process?

(A) Identifying and assessing the Risks of Material Misstatements
(B) Issuing the final audit report
(C) Meeting with the media to announce audit findings
(D) Finalizing the classification of NPAs

Ans :

(A) Identifying and assessing the Risks of Material Misstatements

The text lists 17 stages in a statutory audit. "Identifying and assessing the Risks of Material Misstatements" is listed as the second stage, occurring very early in the process. This foundational step guides the entire audit strategy, determining where the auditor needs to focus their efforts to address potential significant errors in the financial statements.

Oct/Nov 2014

50. In a statutory audit of a bank, how should asset classification be done?

(A) Borrower-wise, considering all facilities of a single borrower together
(B) Facility-wise, treating each loan as a separate entity
(C) Branch-wise, aggregating all assets within a

(C) To handle customer complaints and grievances
(D) To ensure the accuracy and correctness of the books of account

Ans :

(D) To ensure the accuracy and correctness of the books of account
The chapter states that Internal Audit, which is generally undertaken by the bank's own staff or by CA firms, "is aimed at ensuring the accuracy and correctness of the books of account of banks." This is crucial for maintaining public confidence, as banks depend on the trust of the public who deposit their money.

Oct/Nov 2008

32. In the context of the changing banking scenario, what should be a central priority for an internal auditor?
(A) Designing new loan products
(B) Detection of frauds
(C) Public relations and brand management
(D) Cross-selling financial products

Ans :

(B) Detection of frauds
The text emphasizes that with the entire banking sector being engulfed by frauds, an auditor's priorities should "centre around detection of frauds inter alia other important objectives." This is especially relevant given the adoption of liberalised policies and sweeping changes in the banking landscape, making fraud detection a critical part of the audit function.

May/June 2006

33. Which of the following is listed as an important aspect to be considered about Internal Audit?
(A) Its role in setting the bank's business targets
(B) Its role in evaluating and improving the effectiveness of Risk Management
(C) Its responsibility for approving large corporate loans
(D) Its function in determining employee salaries and promotions

Ans :

(B) Its role in evaluating and improving the effectiveness of Risk Management
The chapter lists several important aspects of Internal Audit. Among them is the "Role of Risk-Based Internal Audit in evaluating & improving the effectiveness of Risk Management and governance processes." This highlights the modern, strategic role of internal audit beyond just checking transactions and ensuring accuracy, aligning it with the bank's overall governance.

Oct/Nov 2017

34. The increased adoption of technology by banks has given rise to which type of risks, requiring effective management and a specific type of audit?
(A) Credit risks
(B) Market risks
(C) Liquidity risks
(D) Technology related risks

Ans :

(D) Technology related risks
The section on Information Systems (IS) Audit begins by stating that "with the increased technology adoption by Banks, the complexities within the IT environment have given rise to considerable technology related risks requiring effective management." This has necessitated the rise and importance of IS Audit to provide assurance on IT controls.

May/June 2008

35. What is an IS Audit primarily a process of?
(A) Collecting and evaluating evidence to determine how well a computer system is managed
(B) Developing new software for the bank
(C) Training employees on how to use the computer systems
(D) Selling the bank's old hardware and software

Ans :

(A) Collecting and evaluating evidence to determine how well a computer system is managed
IS Audit is defined as "a process of collecting and evaluating evidence/information to determine whether a computer system" can safeguard assets, maintain data integrity, achieve organizational goals, and use resources efficiently. This evaluation provides an independent view on the extent to which technology-related risks are managed, which is crucial for bank management and the RBI.

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(A) A minimum of three years

The RBI instruction regarding the 'Tenor for appointment of Head of Internal Audit' specifies that the HIA should be appointed for a reasonably long period. It preferably recommends a minimum period of three years. This is to ensure stability and allow the HIA to implement and oversee audit strategies effectively over a meaningful timeframe.

May/June 2025

19. According to RBI guidelines, what should be the reporting structure for the Head of Internal Audit (HIA)?

(A) The HIA must report exclusively to the head of the largest business vertical

(B) The HIA must report to the Chief Financial Officer (CFO)

(C) The HIA shall directly report to either the Audit Committee of the Board (ACB) or the MD & CEO/WTD

(D) The HIA shall report to the head of the Human Resources department for performance appraisal

Ans :

(C) The HIA shall directly report to either the Audit Committee of the Board (ACB) or the MD & CEO/WTD

The 'Reporting Line' instruction from the RBI states that the HIA must have a direct reporting line to a high level of authority. This should be either the Audit Committee of the Board (ACB) or the Managing Director & CEO / Whole Time Director (WTD), ensuring the audit function's independence and stature within the bank's governance structure.

Oct/Nov 2019

20. If the MD & CEO is the 'reporting authority' for the HIA, who holds the 'reviewing authority' for the HIA's performance appraisal?

(A) The Audit Committee of the Board (ACB)

(B) The Board of Directors

(C) The Chief Financial Officer (CFO)

(D) An external independent body

Ans :

(A) The Audit Committee of the Board (ACB)

The guidelines specify a clear hierarchy to maintain independence. If the Board allows the MD & CEO to be the 'reporting authority' for the HIA, then the 'reviewing authority' for performance appraisal must be the Audit Committee of the Board (ACB), and the 'accepting authority' shall be the Board itself, creating necessary checks and balances.

May/June 2009

21. What restriction is placed on the Head of Internal Audit (HIA) concerning business activities?

(A) The HIA can be given small, achievable business targets related to improving control environments

(B) The HIA can have a temporary reporting relationship with a business vertical for special projects

(C) The HIA shall not have any reporting relationship with business verticals and shall not be given business targets

(D) The HIA can participate in business development meetings to provide forward-looking audit insights

Ans :

(C) The HIA shall not have any reporting relationship with business verticals and shall not be given business targets

To ensure objectivity and prevent conflicts of interest, the RBI guidelines are very specific. They state that the HIA shall not have any reporting relationship with the business verticals of the bank and, crucially, shall not be given any business targets. This separation ensures the audit function remains independent from the operational performance it is meant to assess.

Oct/Nov 2011

22. How does the remuneration policy for internal audit staff support their independence and objectivity?

(A) By linking their pay directly to the bank's overall profitability to promote a shared corporate goal

(B) By offering performance bonuses based on the number and financial impact of irregularities they uncover

(C) By making their salaries the highest in the bank to ensure their undisputed authority and attract top talent

(D) By structuring it to avoid linkage to the financial performance of the business lines they audit

Ans :

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The chapter lists several critical areas for the application of CAATs. One of these is "Monitoring customer transactions under AML requirements." Anti-Money Laundering compliance involves sifting through vast amounts of transaction data to identify suspicious patterns, a task for which automated techniques like CAATs are particularly well-suited and necessary.

May/June 2022

41. Which audit procedure can be performed using CAATs?
(A) Interviewing senior management about business strategy
(B) Physically inspecting a property held as collateral
(C) Re-calculating entries performed by the entity's accounting systems
(D) Assessing the morale of the employees in a branch

Ans :

(C) Re-calculating entries performed by the entity's accounting systems
A list of audit procedures performable by CAATs is provided. This includes "Re-calculating entries performed by the entity's accounting Systems." This is a classic application where a CAAT can independently verify calculations like interest accrual or amortization across thousands of accounts, ensuring systemic accuracy far more efficiently than manual checks.

Oct/Nov 2023

42. As per the "Guiding Principles of Information Systems (IS) Audit" from the Master Circular dated 26th September 2012, what qualification should professionals in IS Audit Teams ideally have?
(A) CISA qualified
(B) MBA in Finance
(C) Law degree
(D) PhD in Economics

Ans :

(A) CISA qualified
The guiding principles mentioned in the text state that banks should form separate IS Audit Teams with persons having adequate IT experience and who are "suitably CISA qualified professionals." CISA (Certified Information Systems Auditor) is a globally recognized certification for professionals in IS audit, control, and security, indicating a specific, relevant expertise.

Oct/Nov 2025

43. What does the Standard on Internal Audit (SA) 14, issued by the Institute of Chartered Accountants of India, establish?
(A) Standards for financial reporting in banks
(B) Procedures for conducting a statutory audit
(C) Standards on procedures for an internal audit in an IT environment
(D) Ethical guidelines for all bank employees

Ans :

(C) Standards on procedures for an internal audit in an IT environment
The text clearly states that "The Institute of Chartered Accountants of India has issued SA 14 to establish standards on procedures to be followed when an internal audit is conducted in an information technology environment." This standard provides a formal framework and guidance for auditors operating in the increasingly complex IT landscapes of modern businesses.

May/June 2016

44. According to which act are annual financial statements of banks required to be audited?
(A) The Companies Act, 2013
(B) The Reserve Bank of India Act, 1934
(C) The Income-tax Act, 1961
(D) The Banking Regulation Act, 1949

Ans :

(D) The Banking Regulation Act, 1949
The introduction to Statutory Audit specifies that "As per the Banking Regulation Act, 1949, annual Financial Statements in the form of Profit and Loss Account and Balance Sheet are required to be audited in accordance with the requirements of applicable statutes." This act forms the legal basis for the mandatory statutory audit of banks.

Oct/Nov 2009

45. What does the term 'Statute' mean in the context of a 'Statutory Auditor'?
(A) Mandated or compulsorily required by any law or Act
(B) An internal policy of the bank
(C) A recommendation from an industry body
(D) A guideline issued for a specific project

Ans :

NODIA

(A) To identify cases related to leakage of interest and other charges

A Revenue Audit, also known as an Income & Expenditure audit, has a specific focus. The text states it "is aimed at identifying cases related to leakage of interest and other charges." This type of audit helps the bank ensure that it is correctly calculating and collecting all the income it is entitled to.

Oct/Nov 2022

56. A Stock and Receivables Audit is normally conducted for which type of accounts?

(A) All savings bank accounts
(B) Only large borrower accounts
(C) All fixed deposit accounts
(D) All staff loan accounts

Ans :

(B) Only large borrower accounts

The chapter explains that Stock and Receivables Audits are conducted to check the statements submitted by borrowers. It specifies that "Only large borrower accounts are normally are subjected to this audit." This is a risk-based approach, focusing audit resources on accounts with higher exposure where the value of underlying security is significant.

May/June 2018

57. What is the defining purpose of a Forensic Audit?

(A) To provide an opinion on the 'true and fair' view of financial statements
(B) To assess the efficiency of an organization's management
(C) To examine and evaluate financial information for use of evidence in court
(D) To check for leakages in bank revenue and expenditure

Ans :

(C) To examine and evaluate financial information for use of evidence in court

Forensic Audit is distinct from other audits in its objective. It is defined as "an examination and evaluation of a firm's or individual's financial information for use of evidence in court." Its primary purpose is to investigate potential fraud or financial disputes in a manner that will stand up to legal scrutiny.

Oct/Nov 2016

58. What is a key objective of a Management Audit?

(A) To see how far the objectives of management are fulfilled and evaluate its efficiency
(B) To verify the correctness of tax returns submitted by the bank
(C) To ensure every transaction is recorded correctly in the books of account
(D) To provide evidence for use in a court of law

Ans :

(A) To see how far the objectives of management are fulfilled and evaluate its efficiency

A Management Audit assesses the methods and policies of an organization's management. Its main objective "is to see how far the objectives of management are fulfilled." It also "aims to ascertain whether sound management prevails throughout the organisation and evaluates its efficiency in the system of its operation," focusing on overall effectiveness.

May/June 2014

59. What is the purpose of a Tax Audit, including GST Audit?

(A) To determine the future profitability of the business entity
(B) To assess the performance of the management team
(C) To analyze tax returns to see if the tax information and resulting payment is valid
(D) To check the physical stock of goods held by a borrower

Ans :

(C) To analyze tax returns to see if the tax information and resulting payment is valid

The text defines Tax Audit as "an analysis of the tax returns submitted by an individual or business entity, to see if the tax Information and resulting income tax payment is valid." Statutory auditors of banks are mentioned to usually deal with the provision for Taxation & GST, making this audit relevant.

Oct/Nov 2007

60. Identify the incorrect statement from the following options.

(A) A Forensic Audit's primary goal is to give a 'true and fair' opinion.
(B) A Concurrent Audit is contemporaneous with transactions.
(C) A Statutory Audit relies on the work of internal auditors.
(D) A Revenue Audit is aimed at identifying

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single branch
(D) Product-wise, grouping all housing loans or car loans together

Ans :

(A) Borrower-wise, considering all facilities of a single borrower together
The list of stages in a statutory audit provides a specific guideline for asset classification. Stage 17 states, "Asset classification (It should be Borrower-wise and not facility-wise)." This means if a borrower defaults on one loan, all of their other facilities with the bank may also need to be classified as non-performing.

May/June 2019

51. Which type of report is issued by Statutory Auditors as per the requirements of RBI guidelines?
(A) The Concurrent Audit Report
(B) The Internal Audit Report
(C) The Long Form Audit Report (LFAR)
(D) The Management Audit Report

Ans :

(C) The Long Form Audit Report (LFAR)
The chapter lists three types of reports to be issued by Statutory Auditors. One of these is the "Long Form Audit Report (As per the requirements of RBI guidelines)." The LFAR is a detailed questionnaire/report through which the statutory auditor comments on various aspects of the bank's functioning, supplementing the main audit report.

Oct/Nov 2006

52. Who appoints the auditors of Public Sector Banks?
(A) The shareholders at the Annual General Meeting
(B) The Reserve Bank of India directly
(C) Their Board of Directors, as per RBI guidelines
(D) The Institute of Chartered Accountants of India

Ans :

(C) Their Board of Directors, as per RBI guidelines
The text distinguishes between the appointment process for private and public sector banks. It states that "The auditors of Public Sector Banks are appointed by their Board of Directors. (As per RBI guidelines)." This is different from private banks where auditors are appointed by shareholders at the AGM.

May/June 2021

53. Who appoints the auditors of Private Banks?
(A) The Board of Directors of the bank
(B) The Reserve Bank of India
(C) The shareholders at the Annual General Meeting
(D) The Comptroller & Auditor General of India

Ans :

(C) The shareholders at the Annual General Meeting
The chapter clearly outlines the appointment process for auditors in different types of banks based on relevant enactments. It specifies that "The auditors of Private Banks are appointed at the Annual General Meeting of the shareholders," ensuring accountability to the owners of the company.

Oct/Nov 2010

54. The Auditing Standard (SA) 240 deals with which of the following?
(A) Planning an Audit of Financial Statements
(B) Using the work of Another Auditor
(C) Quality Control for an Audit of Financial Statements
(D) The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements

Ans :

(D) The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements
The text provides a list of important Auditing and Review Standards applicable to the audit of financial statements. In this list, SA 240 is explicitly titled "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements," highlighting the specific guidance available to auditors on this critical issue.

May/June 2005

55. What is the primary aim of a Revenue Audit?
(A) To identify cases related to leakage of interest and other charges
(B) To verify the bank's capital adequacy ratio
(C) To assess the effectiveness of the bank's marketing department
(D) To check compliance with HR policies

Ans :

NODIA

independent examination, allowing for the timely detection and rectification of any irregularities.

May/June 2020

27. What is the primary advantage of conducting a Concurrent Audit?
(A) It reduces the need for a statutory audit at the year-end by pre-clearing all transactions
(B) It guarantees that no frauds will ever occur in the branch due to its continuous presence
(C) It primarily helps in improving the bank's marketing strategies by providing real-time customer feedback
(D) It allows irregularities to be found and rectified immediately, preventing them from piling up

Ans :

(D) It allows irregularities to be found and rectified immediately, preventing them from piling up
A key benefit highlighted is that through concurrent audit, irregularities or non-conformities are easily identified as they happen. This allows for immediate rectification, thereby "avoiding the piling up of irregularities which may become a huge problem for any branch when the year-end audit comes around." It acts as a preventive and corrective mechanism.

Oct/Nov 2015

28. Which of the following activities is typically checked by Concurrent Auditors on a daily basis?
(A) Maximum cash balance adherence and KYC norms compliance
(B) The bank's five-year strategic business plan
(C) The appointment process of the bank's Board of Directors
(D) The bank's overall market capitalization and stock performance

Ans :

(A) Maximum cash balance adherence and KYC norms compliance
The text provides specific examples of the scope of a concurrent audit. It states that Concurrent Auditors check items like "daily maximum cash balance adherence compliance, KYC norms compliance, proper documentation of new loan disbursements," and other operational and regulatory aspects. These checks are part of the substantive checking in key areas.

May/June 2013

29. According to the RBI Guidelines on Concurrent Audit System dated 18th September 2019, what is a key purpose of this audit?
(A) To function as a part of the bank's marketing and customer feedback system by interacting with customers daily
(B) To replace the need for internal and statutory audits completely by performing all their functions on a continuous basis
(C) To act as a part of the bank's early warning system for timely detection of serious errors
(D) To evaluate the performance of senior management for remuneration purposes by observing their daily decisions

Ans :

(C) To act as a part of the bank's early warning system for timely detection of serious errors
The RBI guidelines view concurrent audit as integral to sound internal controls. It is regarded as "part of a bank's early warning system to ensure timely detection of serious errors and irregularities." This function also helps in averting fraudulent transactions and contributes to preventive vigilance within the bank, enhancing its overall control environment.

Oct/Nov 2021

30. Which of the following is NOT listed as a subject covered by the revised RBI guidelines on Concurrent Audit?
(A) Technology platform for the audit
(B) Coverage and Appointment of Auditors
(C) Accountability and Tenure
(D) Remuneration and Reporting System

Ans :

(A) Technology platform for the audit
The text lists the areas covered by the revised guidelines on the Concurrent Audit System. These include Coverage, Appointment of Auditors, Accountability, Tenure, Remuneration, Review of effectiveness, and the Reporting System. A specific 'Technology platform for the audit' is not mentioned in this particular list, although technology is relevant to auditing in general.

May/June 2024

31. What is the primary aim of an Internal Audit in a bank?
(A) To set interest rates for loans and deposits
(B) To manage the bank's investment portfolio

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interest leakage.

Ans :

(A) A Forensic Audit's primary goal is to give a 'true and fair' opinion.
The primary goal of a Forensic Audit is to examine financial information for use as evidence in court, often to prove or disprove fraud. The goal of providing a 'true and fair' opinion is the primary objective of a Statutory Audit, not a Forensic Audit, which has a much more specific and investigative focus.

May/June 2025

61. Identify the correct pair from the following.
(A) Concurrent Audit - Conducted annually after year-end
(B) Statutory Audit - Focuses on operational efficiency of management
(C) Revenue Audit - Aims to find leakage of interest and charges
(D) Management Audit - Required by the Banking Regulation Act, 1949

Ans :

(C) Revenue Audit - Aims to find leakage of interest and charges
The text correctly pairs the Revenue Audit with its objective of identifying leakage of interest and other charges. Concurrent audit is contemporaneous, not annual. Statutory audit focuses on financial statements and regulatory compliance, not management efficiency. Management audit is a discretionary assessment, not a statutory requirement under the Banking Regulation Act, 1949.

Oct/Nov 2019

62. Which of the following statements about the role of an audit is correct?
(A) The main objective of audit has always been to ascertain a 'true and fair' view.
(B) An auditor's work is free from the exercise of judgment.
(C) An auditor must check each and every transaction to form an opinion.
(D) Audit provides comfort to users that financial statement information can be relied upon.

Ans :

(D) Audit provides comfort to users that financial statement information can be relied upon.
The text states that an audit "provides comfort to the users of the financial statements of a business that the information available in the statements can be relied upon." This assurance is a key outcome of the audit process. The other statements are incorrect as the audit objective shifted, it involves judgment, and it doesn't check every transaction.

May/June 2009

63. Which of the following statements regarding Risk-Based Internal Audit (RBIA) is incorrect?
(A) RBIA was first introduced in SCBs by an RBI circular in 2002.
(B) RBIA links internal auditing to the organisation's overall risk management framework.
(C) RBIA's focus is on auditing the risks themselves, not the management of risk.
(D) RBIA involves prioritization of audit areas based on risk assessment.

Ans :

(C) RBIA's focus is on auditing the risks themselves, not the management of risk.
The chapter explicitly clarifies this point by stating, "RBIA is not about auditing risks but about auditing the management of risk." It focuses on the processes used by management to handle risks. Therefore, the statement that RBIA's focus is on auditing the risks themselves is incorrect and misrepresents the core philosophy of this modern audit approach.

Oct/Nov 2011

64. Consider the following statements regarding the Head of Internal Audit (HIA):
1. The HIA shall be a senior executive of the bank.
2. The HIA can be appointed for a minimum period of one year.
3. The HIA can be given business targets to align audit with business goals.

Which of the above statements is/are correct?
(A) 1 only
(B) 1 and 2 only
(C) 2 and 3 only
(D) 1, 2, and 3

Ans :

(A) 1 only
According to RBI instructions, the HIA must be a senior executive (Statement 1 is correct). The

NODIA

established rules and guidelines, which is crucial for financial stability.

May/June 2007

90. The RBI circular dated January 07, 2021, supplemented the framework for which type of audit?
(A) Risk-Based Internal Audit (RBIA)
(B) Statutory Audit
(C) Concurrent Audit
(D) Tax Audit

Ans :

(A) Risk-Based Internal Audit (RBIA)
The chapter mentions that the RBI introduced the RBIA system in 2002. It then explicitly states, "This was further supplemented vide circular dated January 07, 2021." This indicates that the 2021 circular provided additional guidelines and reinforced the framework for Risk-Based Internal Audit, building upon the initial introduction from 2002.

May/June 2012

91. Based on the provided definition, what does an audit aim to safeguard the proprietor against?
"The book 'An Introduction to Indian Government Accounts and Audit' issued by the Comptroller and Auditor General of India, defines audit as: 'An instrument of financial control. It acts as a safeguard on behalf of the proprietor (whether an individual or group of persons) against extravagance, carelessness or fraud on the part of the proprietor's agents or servants... and it ensures on the proprietor's behalf that the accounts maintained truly represent facts and that the expenditure has been incurred with due regularity and propriety.'"
(A) Business competition and market downturns
(B) Poor strategic decisions made by the proprietor
(C) Technological obsolescence and innovation risks
(D) Extravagance, carelessness, or fraud by agents or servants

Ans :

(D) Extravagance, carelessness, or fraud by agents or servants
The provided definition explicitly states that audit acts as a safeguard against "extravagance, carelessness or fraud on the part of the proprietor's agents or servants." This highlights the audit's role in monitoring those entrusted with managing the proprietor's assets and financial affairs, ensuring they act responsibly and honestly in their duties.

Oct/Nov 2014

92. If a bank's Board decides that the MD & CEO will be the 'reporting authority' for the Head of Internal Audit (HIA), who is responsible for being the 'reviewing authority' in the HIA's performance appraisal?
"(e) Reporting Line - The HIA shall directly report to either the Audit Committee of the Board (ACB) / MD & CEO or Whole Time Director (WTD). Should the Board of Directors decide to allow the MD & CEO or a WTD to be the 'reporting authority' of the HIA, then the 'reviewing authority' shall be with the ACB and the 'accepting authority' shall be with the Board in matters of performance appraisal of the HIA."
(A) The MD & CEO himself
(B) The Audit Committee of the Board (ACB)
(C) The Board of Directors
(D) An external HR consultant

Ans :

(B) The Audit Committee of the Board (ACB)
The excerpt provides a clear procedural rule to maintain checks and balances. It specifies that if the MD & CEO is designated as the 'reporting authority' for the HIA, then the responsibility for performance review shifts upwards. In this scenario, the 'reviewing authority' must be the Audit Committee of the Board (ACB).

May/June 2019

93. According to the excerpt, what kind of checking is emphasized in Concurrent Audit?
"It is a continuous audit, which goes on all the year around, usually conducted by external auditors (chartered accountants) on a monthly basis. In Concurrent Audit, daily basic transactions are examined and checked. This ensures that any irregularities are nipped in the bud. There is an emphasis in favour of substantive checking in Key areas rather than test checking."
(A) Test checking of all areas equally
(B) Checking only year-end balances
(C) Substantive checking in Key areas
(D) A quick review without detailed checks

Ans :

(C) Substantive checking in Key areas

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(D) The auditor has to depend on explanations by the management.

Ans :

(A) The auditor is required to ensure the future viability of the business.

An audit focuses on historical financial information to provide an opinion on its truth and fairness. It does not and cannot guarantee the future viability of the business. The other three options—expressing an opinion, exercising professional judgment, and depending on management explanations—are all explicitly mentioned as inherent limitations of the audit process.

May/June 2020

69. The shift from 'auditing around the computer' to 'auditing through the computer' signifies what?

(A) A decrease in the importance of technology in auditing.
(B) A return to manual auditing methods.
(C) A move towards using the computer itself as a tool to perform audit tests.
(D) A focus on auditing only the physical components of a computer system.

Ans :

(C) A move towards using the computer itself as a tool to perform audit tests.

'Auditing around the computer' involved checking inputs and outputs but ignoring the internal processing. 'Auditing through the computer' involves using computer-aided techniques to test the system's internal controls and process data directly. This represents a deeper, more integrated use of technology as an essential tool in the audit process itself.

Oct/Nov 2015

70. Which of the following statements about the internal audit function's competence is correct as per RBI guidelines?

(A) Banks should ensure the internal audit function has the requisite skills to audit all areas of the bank.
(B) Internal auditors only need core expertise in accounting, as other skills can be outsourced.
(C) Forensic investigation skills are considered outside the scope of internal audit and are handled by a separate department.
(D) Competence is desirable, but not as essential as strict adherence to the audit schedule for an effective function.

Ans :

(A) Banks should ensure the internal audit function has the requisite skills to audit all areas of the bank.

The RBI instruction on 'Competence' is comprehensive. It states that banks should ensure the internal audit function has the necessary skills to audit all areas. It explicitly mentions a wide range of desired knowledge, including banking operations, accounting, IT, data analytics, and forensic investigation, making the other options incorrect or incomplete.

May/June 2013

71. What is the RBI's guidance on staff rotation in the Internal Audit function?

(A) Staff should be permanently assigned to the internal audit function for their entire career.
(B) Staff rotation in the audit function is discouraged to maintain expertise.
(C) Only staff without specialized knowledge should be rotated into the audit function.
(D) The Board should prescribe a minimum period of service for staff in the Internal Audit function.

Ans :

(D) The Board should prescribe a minimum period of service for staff in the Internal Audit function.

The guideline on 'Staff Rotation' suggests that, except for career internal auditors in specialized functions, the Board should prescribe a minimum service period for staff in Internal Audit. This ensures a balance between gaining experience and bringing fresh perspectives, while also suggesting bringing in staff with specialized knowledge for at least one stint.

Oct/Nov 2021

72. Consider the following statements about the reporting line of the HIA in foreign banks operating in India as branches:

1. The HIA reports to the MD & CEO of the Indian operations.
2. The HIA reports to the Audit Committee of the Board in India.
3. The HIA reports to the internal audit function in the controlling office/head office.

Which statement is correct?

(A) 1 only

NODIA

May/June 2005

97. According to the definition provided, what is a key aim of a Forensic Audit?
"Concept of Forensic Audit may be defined as 'A concentrated audit of all the transactions of the entity to find the correctness of such transactions and to report whether or not any financial benefit has been attained by way of presenting an unreal picture. This audit aims at determining whether fraud has actually occurred or not.'"
(A) To provide suggestions for improving operational efficiency.
(B) To give an opinion on the true and fair view of the accounts.
(C) To check for compliance with priority sector lending norms.
(D) To determine if fraud has actually occurred.

Ans :

(D) To determine if fraud has actually occurred.
The provided text defines forensic audit as a concentrated examination aimed at finding correctness and reporting on illicit financial benefits. It explicitly states, "This audit aims at determining whether fraud has actually occurred or not." This investigative purpose is what distinguishes it from a general financial or compliance audit.

Oct/Nov 2022

98. Question 98. A bank's internal audit department lacks expertise in complex derivative products. What action is permissible under the outsourcing guideline?
"Outsourcing - The internal audit function shall not be outsourced. However, where required, experts, including former employees, could be hired on contractual basis subject to the ACB being assured that such expertise does not exist within the audit function of the bank. ... Ownership of audit reports in all cases shall rest with regular functionaries of the internal audit function."
(A) The bank can hire an external expert on a contractual basis, provided the ACB approves.
(B) The bank can outsource its entire internal audit function to a specialized firm.
(C) The bank must train its existing staff and cannot hire any external help.
(D) The external expert, if hired, will have final ownership of the audit report.

Ans :

(A) The bank can hire an external expert on a contractual basis, provided the ACB approves.
The guideline prohibits outsourcing the entire function but allows for hiring experts contractually. This is subject to the Audit Committee of the Board (ACB) being assured that the required expertise is not available internally. The ownership of the report remains with the bank's internal audit function, ensuring accountability is not outsourced.

May/June 2018

99. Question 99. What responsibility is placed upon Branch Managers regarding IS audit as per the guiding principles?
"Branch Managers should submit Compliance of DO's and Don'ts regarding IS audit key areas, on monthly basis."
(A) To conduct the IS audit of their own branch.
(B) To develop the bank's overall IS Audit Policy.
(C) To submit a monthly compliance report on key IS audit areas
(D) To hire CISA qualified professionals for the bank.

Ans :

(C) To submit a monthly compliance report on key IS audit areas
The source text clearly outlines a specific, recurring responsibility for Branch Managers. It states they "should submit Compliance of DO's and Don'ts regarding IS audit key areas, on monthly basis." This makes branch management directly accountable for implementing and adhering to basic IT controls and procedures at the operational level.

Oct/Nov 2016

100. Based on the description, a management audit would most likely evaluate which of the following?
"Management Audit is an assessment of methods and policies of an organisation's management in the administration and the use of resources, tactical and strategic planning and employee and organisational improvement. The main objective of management audit is to see how far the objectives of management are fulfilled."
(A) The effectiveness of the management's strategic planning process.
(B) The accuracy of interest calculation on

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May/June 2008

77. In carrying out substantive procedures, what is the statutory auditor's approach to examining advances?
(A) Examine only a small sample of large advances and all other advances.
(B) Examine only advances that have become NPAs.
(C) Examine all advances without any sampling.
(D) Examine all large advances and a sample of other advances.

Ans :

(D) Examine all large advances and a sample of other advances.
The chapter outlines the practical approach for statutory auditors. It states, "In carrying out his Substantive procedures, the auditor should examine all large advances while other advances may be examined on a sampling basis." This is a risk-based approach, focusing comprehensive effort on high-value items and using sampling for lower-value, voluminous items.

Oct/Nov 2013

78. Which Auditing Standard (SA) is concerned with "Agreeing to the terms of Audit Engagement"?
(A) SA 210
(B) SA 300
(C) SA 220
(D) SA 510

Ans :

(A) SA 210
The text provides a list of ten important Auditing Standards prescribed by the ICAI that are applicable to financial statement audits. In this list, SA 210 (Revised) is explicitly identified as "Agreeing to terms of Audit Engagement," which deals with the preconditions for an audit and the agreement between the auditor and management.

May/June 2015

79. What is the main objective of a forensic audit concerning fraud?
(A) To prevent any future possibility of fraud.
(B) To provide a general assurance that the financial statements are free from fraud.
(C) To determine whether fraud has actually occurred and to name the persons involved.
(D) To assess the overall risk of fraud in the organization.

Ans :

(C) To determine whether fraud has actually occurred and to name the persons involved.
A forensic audit has a specific investigative mandate. The text states that this audit "aims at determining whether fraud has actually occurred or not. It also aims the naming of persons involved." This goes beyond general risk assessment and seeks to establish facts about a specific suspected wrongdoing for potential legal action.

Oct/Nov 2012

80. Which of the following is NOT a type of audit report issued by Statutory Auditors as mentioned in the text?
(A) Risk Management Audit Report
(B) Statutory Audit Report (as per SA 700/705/706)
(C) Long Form Audit Report (LFAR)
(D) Tax Audit Report (as per Income-tax Act, 1961)

Ans :

(A) Risk Management Audit Report
The chapter lists three specific types of reports issued by Statutory Auditors: the main Statutory Audit Report, the Long Form Audit Report (LFAR) for RBI, and the Tax Audit Report. A "Risk Management Audit Report" is not mentioned as a distinct, formal report type issued by statutory auditors in this context.

May/June 2011

81. Which entity's inputs, besides those from ICAI, are obtained by the RBI before finalising the panel of Chartered Accountants for statutory bank audits?
(A) Securities and Exchange Board of India (SEBI)
(B) Comptroller & Auditor General of India (CAG)
(C) Ministry of Finance
(D) Indian Banks' Association (IBA)

Ans :

(B) Comptroller & Auditor General of India (CAG)
The text states that when RBI prepares the panel of eligible Chartered Accountants for bank audits, it uses data from the Institute of Chartered Accountants of India (ICAI). It explicitly adds,

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recommended minimum tenor is three years, not one year (Statement 2 is incorrect). The HIA shall not be given any business targets to maintain independence (Statement 3 is incorrect). Therefore, only the first statement is correct.

May/June 2010

65. Consider the following statements:
Statement I : The internal audit function in a bank can be fully outsourced to an external agency to improve efficiency.
Statement II : Ownership of audit reports shall always rest with the regular functionaries of the bank's internal audit function, even if external experts are hired.
(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Statement I is correct, but Statement II is incorrect.
(D) Statement I is incorrect, but Statement II is correct.

Ans :

(D) Statement I is incorrect, but Statement II is correct.
The RBI guidelines state that the internal audit function shall not be outsourced, making Statement I incorrect. However, experts can be hired on a contractual basis. The guidelines further specify that ownership of audit reports in all cases rests with the regular internal audit functionaries, making Statement II correct. This ensures internal accountability.

Oct/Nov 2024

66. **Assertion (A) :** The remuneration of internal audit staff should not be linked to the financial performance of the business lines they audit.
Reason (R) : Linking remuneration to business line performance could compromise the independence and objectivity of the internal audit function.
(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
The text explicitly states that remuneration policies should be structured to avoid creating a conflict of interest. The assertion is a direct guideline mentioned. The reason provides the precise logic behind this guideline, which is to prevent the undermining of audit independence and objectivity. Thus, both the assertion and reason are true and the reason correctly explains the assertion.

May/June 2017

67. Match List-I (Type of Audit) with List-II (Primary Objective).
List-I
P. Statutory Audit
Q. Concurrent Audit
R. Forensic Audit
S. Management Audit
List-II
1. Contemporaneous examination of transactions
2. Evaluation of management efficiency and policies
3. Examination of information for use as evidence in court
4. Opinion on 'true and fair' view of financial statements
Select the correct code:
(A) P-4, Q-1, R-3, S-2
(B) P-1, Q-4, R-2, S-3
(C) P-4, Q-3, R-1, S-2
(D) P-2, Q-1, R-3, S-4

Ans :

(A) P-4, Q-1, R-3, S-2
Based on the chapter content: Statutory Audit (P) aims to provide an opinion on the 'true and fair' view (4). Concurrent Audit (Q) is a contemporaneous examination (1). Forensic Audit (R) is for collecting evidence for court (3). Management Audit (S) evaluates management's efficiency and fulfillment of objectives (2).

Oct/Nov 2005

68. Which of the following is NOT an inherent limitation of an audit?
(A) The auditor is required to ensure the future viability of the business.
(B) The auditor can only express an opinion and not a certificate of absolute correctness.
(C) The auditor's work involves the exercise of professional judgment.

NODIA

regulatory provisions (Statement 1 is correct). However, an audit provides an opinion on past performance and does not guarantee future profitability (Statement 3 is incorrect).

May/June 2016

86. Consider the following statements about IS Audit:

1. It aims to determine if a system can maintain data integrity.
2. It evaluates the efficient use of available Information System resources.
3. It is primarily concerned with the physical security of bank branches.
4. It provides an independent and objective view of how well IT risks are managed.

Which combination of statements is correct?

(A) 1, 2, and 3
(B) 1, 2, and 4
(C) 2, 3, and 4
(D) 1, 3, and 4

Ans :

(B) 1, 2, and 4
The chapter defines IS audit's objectives as ensuring data integrity (1), efficient use of resources (2), safeguarding assets, and achieving goals. It provides an independent view on risk management (4). It is not primarily concerned with the physical security of branches (3), but rather the security of IT assets like hardware, software, and data.

Oct/Nov 2009

87. Which of the following is NOT listed as a stage in a statutory audit?

(A) Assessment of ability to continue as Going Concern
(B) Assessing the Risks of Fraud including Money Laundering
(C) Developing the Marketing Plan for the bank
(D) Classification of NPAs based on the record of recovery

Ans :

(C) Developing the Marketing Plan for the bank
The chapter provides a detailed list of 17 stages in a statutory audit. This list includes assessing going concern, assessing fraud risks, and classifying NPAs. Developing a marketing plan is a management function related to business development and is not part of the statutory audit process, which focuses on financial reporting and compliance.

May/June 2023

88. **Assertion (A) :** The emergence of Risk-Based Internal Audit (RBIA) shifted the focus of internal audit in banks.
Reason (R) : Historically, bank internal audits concentrated on transaction testing and accuracy, but the changing scenario required evaluation of risk management procedures and internal controls.

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
The assertion that RBIA shifted the focus is a key theme of the chapter. The reason perfectly explains this shift by contrasting the historical focus (transaction testing) with the new focus (evaluating risk management). The text directly supports that this change was a response to the evolving and more complex banking environment.

Oct/Nov 2018

89. What is the most appropriate description of bank audit?

(A) A one-time check conducted only when a fraud is suspected.
(B) An optional activity that banks can choose to undertake for self-improvement.
(C) A routine procedure to ensure compliance with industry standards and regulatory norms.
(D) A process focused solely on improving the bank's customer service.

Ans :

(C) A routine procedure to ensure compliance with industry standards and regulatory norms.
The text describes bank audit as "the routine procedure that all banks must undergo in order to ensure that they are in compliance with industry standards and regulatory norms." This definition emphasizes its mandatory, regular nature and its core purpose of ensuring adherence to

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(B) 2 only
(C) 3 only
(D) 1 and 2

Ans :

(C) 3 only
The text provides a specific rule for foreign banks. It states, "In foreign banks operating in India as branches, the HIA shall report to the internal audit function in the controlling office / head office." This ensures that the audit function of the Indian branch is integrated into the global audit governance structure of the parent bank.

May/June 2024

73. Why is quality bank audit considered crucial for the banking sector?
(A) It helps banks design more competitive products.
(B) It is the primary tool for marketing and building a brand image.
(C) It ensures the banking sector stays healthy, safe, and stable.
(D) It directly increases the bank's stock price.

Ans :

(C) It ensures the banking sector stays healthy, safe, and stable.
The text emphasizes the systemic importance of the banking sector for the economy's stability. It states, "It is important that the banking sector stays healthy, safe and stable. Quality bank audit plays a crucial role to ensure this." Reliable financial information, supported by quality audits, is a cornerstone of this stability and public confidence.

Oct/Nov 2008

74. What is the primary purpose of the documentation requirement in the RBI guidelines for RBIA?
(A) To increase the amount of paperwork for auditors, ensuring a detailed trail for every action taken
(B) To create a comprehensive training manual for new employees in the business departments
(C) To prepare a standardized report specifically for submission to the stock exchange and other regulators
(D) To demonstrate that the RBIA framework captures all significant criteria suited for the bank's structure and risks

Ans :

(D) To demonstrate that the RBIA framework captures all significant criteria suited for the bank's structure and risks
The 'Documentation' guideline requires banks to "ensure and demonstrate through proper documentation that their risk-based internal audit framework captures all the significant criteria / principles suited for their organisational structure, the business model and the risks." This serves as evidence of a well-designed and tailored RBIA process.

May/June 2006

75. Which type of audit is described as a "continuous audit, which goes on all the year around"?
(A) Concurrent Audit
(B) Statutory Audit
(C) Forensic Audit
(D) Management Audit

Ans :

(A) Concurrent Audit
The chapter describes Concurrent Audit using these exact terms. It is defined as a continuous process that happens throughout the year, unlike a statutory audit which is typically a year-end activity. This continuous nature allows for the ongoing and timely examination of transactions, making it a powerful control mechanism for banks.

Oct/Nov 2017

76. According to the guiding principles for IS Audit, what should become an essential part of Internal Audit in the post-CBS scenario?
(A) Manual transaction checking
(B) IS Audit
(C) Customer feedback surveys
(D) Marketing and sales review

Ans :

(B) IS Audit
The Master Circular on Audit Systems lays down guiding principles. One of these principles is that "IS Audit should become essential part of Internal Audit in the post CBS scenario." With Core Banking Solutions (CBS) being central to bank operations, auditing the underlying IT systems and controls becomes fundamentally important for the overall internal audit function.

NODIA

The text explicitly contrasts the approach used in Concurrent Audit with other methods. It states, "There is an emphasis in favour of substantive checking in Key areas rather than test checking." This means the audit involves in-depth verification of transactions and balances in critical operational areas rather than just sampling across the board.

Oct/Nov 2006

94. Based on the excerpt, which of the following falls outside the scope of determination for an IS Audit?

"IS Audit is a process of collecting and evaluating evidence/information to determine whether a computer system could:

1. safeguard its assets (hardware, software and data) through adoption of adequate security control measures.
2. maintain data integrity.
3. achieve goals of the organisation effectively; and.
4. result in the efficient use of the available information System resources."

(A) The system's ability to maintain data integrity
(B) The system's role in achieving organizational goals
(C) The system's efficiency in using available resources
(D) The system's contribution to the bank's marketing budget

Ans :

(D) The system's contribution to the bank's marketing budget

The excerpt lists four specific determinations of an IS Audit: safeguarding assets, maintaining data integrity, achieving organizational goals, and ensuring efficient use of resources. The system's contribution to the marketing budget is a financial allocation matter, not a core objective of an IS audit as defined in the provided text.

May/June 2021

95. Based on the excerpt, on what does a statutory auditor primarily rely to form an opinion, instead of examining transaction intricacies?

"Statutory audit does not look at the intricacies of the banking transactions (which are looked into by concurrent and Internal audits); instead they rely on the concurrent audit & internal Audit Reports and test checking to form their opinion. Statutory audit mainly looks at the loans and advances, Compliance with Priority Sector Lending (PSL) requirements, CRR, SLR, CRAR etc."

(A) Concurrent and Internal Audit Reports, along with test checking
(B) Media reports and public perception
(C) The bank's marketing and sales figures
(D) Interviews with low-level employees only

Ans :

(A) Concurrent and Internal Audit Reports, along with test checking

The excerpt clearly states the statutory auditor's methodology. Instead of re-examining all transaction details, "they rely on the concurrent audit & internal Audit Reports and test checking to form their opinion." This indicates a hierarchical audit process where the statutory auditor leverages the work done by other continuous and internal audit functions.

Oct/Nov 2010

96. Question 96. A borrower has three loan facilities with a bank: a cash credit account, a term loan, and a car loan. The term loan becomes non-performing. According to the principle mentioned in the source, how should the bank's statutory auditor view the asset classification?

"Asset classification should be borrower-wise and not facility-wise."

(A) Only the term loan should be classified as an NPA.
(B) The classification should be borrower-wise, potentially affecting all three facilities.
(C) The classification should be facility-wise, keeping the other two loans as standard.
(D) The car loan should be exempt from NPA classification.

Ans :

(B) The classification should be borrower-wise, potentially affecting all three facilities.

The source provides a clear directive: asset classification must be "Borrower-wise and not facility-wise." This means the status of the borrower as a whole is considered. If one significant facility turns non-performing, the auditor must ensure that all facilities granted to that same borrower are appropriately classified, likely as NPA, reflecting the overall credit weakness.

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"Inputs of Comptroller & Auditor General of India are also obtained before finalising the list," indicating the CAG's role in this selection process.

Oct/Nov 2020

82. Which of the following is an example of an analytical review procedure that can be performed using CAATs?
(A) Identifying inconsistencies or significant fluctuations in data.
(B) Extracting data for audit testing using sampling programs.
(C) Testing the functioning of a programmed application control.
(D) Performing penetration testing on the network.

Ans :

(A) Identifying inconsistencies or significant fluctuations in data.
The text lists several audit procedures that can be performed using CAATs. "Analytical Review procedures, such as identifying inconsistencies or significant fluctuations" is mentioned as one such procedure. This involves using software to analyze large datasets to spot trends, anomalies, and outliers that might indicate errors or irregularities requiring further investigation.

May/June 2022

83. What is the chronological order of the following stages in a statutory audit?
1. Developing the Audit Plan
2. Identifying and assessing the Risks of Material Misstatements
3. Establishing the overall Audit strategy
4. Preparation of Audit Planning Memorandum

(A) 1, 2, 3, 4
(B) 2, 1, 4, 3
(C) 3, 2, 1, 4
(D) 2, 3, 1, 4

Ans :

(D) 2, 3, 1, 4
According to the list of stages in a statutory audit provided in the chapter, the logical sequence is: first, Identifying Risks (Stage 2); then, Establishing the overall Strategy based on those risks (Stage 5); followed by Developing the detailed Plan (Stage 6); and finally, documenting this in a Memorandum (Stage 7).

NODIA

Oct/Nov 2023

84. Match the Auditing Standard (SA) number from List-I with its subject matter from List-II.
List-I (SA Number)
P. 220 (Revised)
Q. 299
R. 250
S. 330
List-II (Subject Matter)
1. Responsibility of Joint Auditors
2. The Auditors Responses to Assessed Risks
3. Quality Control for an Audit of Financial Statements
4. Consideration of Laws and Regulations in an Audit of Financial Statements

Select the correct code:
(A) P-3, Q-1, R-4, S-2
(B) P-1, Q-3, R-2, S-4
(C) P-3, Q-2, R-4, S-1
(D) P-4, Q-1, R-3, S-2

Ans :

(A) P-3, Q-1, R-4, S-2
According to the list of Auditing Standards provided in the chapter: SA 220 (P) relates to Quality Control (3). SA 299 (Q) relates to the Responsibility of Joint Auditors (1). SA 250 (R) relates to the Consideration of Laws and Regulations (4). SA 330 (S) relates to the Auditor's Responses to Assessed Risks (2).

Oct/Nov 2025

85. Consider the following regarding the scope of a bank audit:
1. It is meant to cross-check that applicable regulatory provisions have been adhered to.
2. It involves a systematic examination of the books of account and records.
3. It guarantees that the bank will be profitable in the future.

Which of the statements is/are correct?
(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(A) 1 and 2 only
The text defines audit as a systematic and scientific examination of books and records (Statement 2 is correct). It also states that audit is meant to cross-check adherence to applicable

savings accounts.
(C) The compliance with SLR and CRR norms.
(D) The correctness of the tax returns filed by the bank.

Ans :

(A) The effectiveness of the management's strategic planning process.
The description defines management audit as an assessment of management's methods, policies, and planning. Evaluating the effectiveness of the strategic planning process falls directly within this scope. The other options relate to operational accuracy, statutory compliance, and tax compliance, which are the domains of other types of audits.

May/June 2014

101. A bank's Board of Directors is considering the appointment of a new Head of Internal Audit (HIA). One candidate is a very successful head of a large business vertical, known for consistently exceeding targets. Another is a senior executive from the risk management department. Based on the RBI guidelines mentioned in the chapter, why might appointing the head of the business vertical as HIA be problematic?
(A) They may lack the seniority required for the role.
(B) They are likely to be less experienced than the risk management candidate.
(C) RBI guidelines prohibit giving the HIA any business targets, creating a conflict with their past role.
(D) RBI guidelines mandate that the HIA must be an external appointment.

Ans :

(C) RBI guidelines prohibit giving the HIA any business targets, creating a conflict with their past role.
The chapter states that the HIA "shall not be given any business targets" and "shall not have any reporting relationship with the business verticals." Appointing a person whose entire career is focused on achieving business targets creates a significant conflict of interest and goes against the principle of maintaining the audit function's independence from business operations.

Oct/Nov 2007

102. An internal auditor at a bank is conducting an audit using the Risk-Based Internal Audit (RBIA) methodology. The auditor spends significant time reviewing the processes and reports used by the credit risk department to identify, measure, and monitor default risk in their loan portfolio. The auditor's actions are an example of which core principle of RBIA?
(A) Auditing the management of risk by focusing on the process applied by the team.
(B) Auditing risks themselves by recalculating the risk of every single loan.
(C) Focusing on full-scale transaction testing of all loan disbursements.
(D) Prioritizing audit areas based on historical transaction volume, not risk.

Ans :

(A) Auditing the management of risk by focusing on the process applied by the team.
The chapter emphasizes that RBIA is "about auditing the management of risk." The auditor in this case is not auditing the risks directly but is reviewing the department's processes for managing risk. This aligns perfectly with the RBIA philosophy of evaluating the effectiveness of the management team's response to risks.

May/June 2025

103. A concurrent auditor at a large branch notices on a particular day that a new high-value term loan was disbursed without obtaining a mandatory valuation report for the property offered as collateral. The auditor immediately includes this finding in their report. What primary objective of concurrent audit is being fulfilled in this scenario?
(A) Evaluating the bank's overall capital adequacy.
(B) Assessing the long-term strategic plan of the bank.
(C) Shortening the interval between a transaction and its examination to find irregularities quickly.
(D) Verifying the bank's compliance with income tax regulations.

Ans :

(C) Shortening the interval between a transaction and its examination to find irregularities quickly.

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Which of the above statements are correct?
(A) 1 and 2 only
(B) 3 and 4 only
(C) 1, 2 and 3 only
(D) All of the above

Ans :

(A) 1 and 2 only
The text states that detection and prevention of fraud is an incidental objective (Statement 1 is correct) and that the auditor's work involves judgment (Statement 2 is correct). It also lists the inability to check every transaction and the fact that an audit provides reasonable, not absolute, assurance as inherent limitations (Statements 3 and 4 are incorrect).

Oct/Nov 2012

122. **Assertion (A) :** The scope of internal audit has widened from historical transaction testing.
Reason (R) : The widening is to evaluate the adequacy and effectiveness of risk management procedures and internal control systems adopted by banks.
(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
The chapter explicitly states that the scope of internal audit has widened. It then explains that this widening was to "evaluate the adequacy and effectiveness of risk management procedures and internal control systems." Therefore, the reason correctly and directly explains the assertion, describing the nature of the change in scope.

May/June 2011

123. Match List-I (Concept) with List-II (Description).
List-I
P. CAATs
Q. RBIA
R. IS Audit
S. Concurrent Audit
List-II
1. Methodology linking audit to the overall risk management framework.
2. Contemporaneous examination of transactions.
3. Techniques to process data of audit significance and improve efficiency.
4. Process to determine if a computer system safeguards assets and maintains data integrity.
Select the correct code:
(A) P-3, Q-1, R-4, S-2
(B) P-2, Q-4, R-1, S-3
(C) P-3, Q-2, R-4, S-1
(D) P-4, Q-1, R-3, S-2

Ans :

(A) P-3, Q-1, R-4, S-2
Based on the chapter's definitions: CAATs (P) are techniques to process data (3). RBIA (Q) is a methodology linking audit to risk management (1). IS Audit (R) evaluates computer systems' controls and integrity (4). Concurrent Audit (S) is a contemporaneous examination of transactions (2).

Oct/Nov 2020

124. Which of the following statements regarding the appointment of auditors for different banks is correct?
(A) Auditors for both Private Sector Banks and Public Sector Banks are appointed by the RBI.
(B) Auditors for Private Banks are appointed by their Board of Directors, while for PSBs they are appointed by shareholders.
(C) Auditors for all banks are appointed by the Comptroller & Auditor General of India.
(D) Auditors for Private Banks are appointed by shareholders at the AGM, while for PSBs they are appointed by their Board of Directors.

Ans :

(D) Auditors for Private Banks are appointed by shareholders at the AGM, while for PSBs they are appointed by their Board of Directors.
The chapter makes a clear distinction. It states, "The auditors of Private Banks are appointed at the Annual General Meeting of the shareholders," and "The auditors of Public Sector Banks are appointed by their Board of Directors. (As per RBI guidelines)." This correctly reflects the different governance and ownership structures.

May/June 2022

125. Which of the following is NOT a stage in Statutory Audit as per the list provided?

NODIA

(B) Compliance tests of general controls
(C) Sampling programmes to extract data for audit testing
(D) Test of transactions and balances, such as recalculating interest

Ans :

(D) Test of transactions and balances, such as recalculating interest
The chapter provides a list of procedures that can be performed by CAATs. The scenario described—recalculating interest on a large scale—directly corresponds to the listed procedure: "Test of transactions and balances, such as recalculating interest." This demonstrates the power of CAATs in performing substantive tests on large volumes of data efficiently and effectively.

Oct/Nov 2024

108. The Board of a bank appoints a Head of Internal Audit (HIA) for a term of three years. His remuneration package includes a significant bonus component that is directly tied to the profitability of the corporate banking division, which he is responsible for auditing. Which RBI guideline for RBIA is being violated in this scenario?
(A) The guideline on Remuneration.
(B) The guideline on the Tenor for appointment of HIA.
(C) The guideline on the Reporting Line of the HIA.
(D) The guideline on Staff Rotation.

Ans :

(A) The guideline on Remuneration.
The tenor of three years is appropriate. However, the chapter's section on 'Remuneration' clearly states that the independence and objectivity of internal audit could be undermined if their remuneration is linked to the financial performance of the business lines they audit. This creates a conflict of interest, which the guideline aims to prevent.

May/June 2017

109. A statutory auditor of a bank is in the process of "Establishing the overall Audit strategy." The bank has a very high volume of transactions in retail lending but a few very large, complex derivative exposures in its treasury department. In line with modern audit principles, where should the auditor's strategy likely focus the most intensive audit effort?
(A) Equally on both retail lending and treasury derivatives.
(B) Primarily on retail lending due to the high volume of transactions.
(C) Primarily on the high-risk, complex treasury derivatives, despite lower volume.
(D) On areas where the internal audit reports are unavailable.

Ans :

(C) Primarily on the high-risk, complex treasury derivatives, despite lower volume.
Modern auditing, including statutory audits, is risk-based. The stage of "Identifying and assessing the Risks of Material Misstatements" precedes strategy development. Complex, high-value derivatives represent a higher risk of material misstatement than high-volume, low-value retail loans. Therefore, the audit strategy would focus more intensive effort on the higher-risk area.

Oct/Nov 2005

110. A bank is suspected of creating fictitious transactions to inflate its revenue figures to secure a large investment. A special audit is commissioned with the specific goal of investigating these transactions to find evidence of the manipulation for a potential legal case. What type of audit is being commissioned in this situation?
(A) Forensic Audit
(B) Revenue Audit
(C) Statutory Audit
(D) Internal Audit

Ans :

(A) Forensic Audit
The scenario's objective is to find evidence of fraud ("fictitious transactions to inflate revenue") for potential legal action. This aligns perfectly with the definition of a Forensic Audit, which is an "examination and evaluation of a firm's... financial information for use of evidence in court" and aims to determine if fraud has occurred.

May/June 2020

111. The introduction of Risk-Based Internal Audit (RBIA) was supplemented by an RBI circular on which date?
(A) December 27, 2002

NODIA

Concurrent audit is contemporaneous. By checking the transaction shortly after it occurred, the auditor identified a critical non-conformity (missing valuation report). This allows for immediate rectification (e.g., getting the report or holding disbursement), "nipping the irregularity in the bud" and preventing a potential future problem, which is a core goal of concurrent audit.

Oct/Nov 2019

104. A bank's Audit Committee of the Board (ACB) decides to hire a firm of cybersecurity experts on a one-year contract to conduct a specialized audit of the bank's defenses against cyber fraud, as the internal team lacks this niche skill. This action is permissible under RBI guidelines on outsourcing internal audit provided that:

(A) The cybersecurity firm takes full ownership of the final audit report.
(B) The entire internal audit function is also handed over to the same firm.
(C) The experts are hired as permanent employees of the bank.
(D) The ACB is assured that this expertise does not exist within the bank's current audit function.

Ans :

(D) The ACB is assured that this expertise does not exist within the bank's current audit function.
The chapter states that while the internal audit function cannot be outsourced, experts can be hired contractually. The key condition is that "the ACB being assured that such expertise does not exist within the audit function of the bank." The ownership of the report must remain with the bank's internal auditors, not the external experts.

May/June 2009

105. A statutory auditor is reviewing the asset classification of a corporate borrower. The bank's records show the borrower's account was regularized just one day before the balance sheet date by a single large credit. The auditor decides to investigate the source of this credit. The auditor's action is consistent with which principle mentioned in the stages of statutory audit?

(A) The auditor should not assume system-generated information is correct without evidence.
(B) Asset classification should be facility-wise.
(C) Classification of NPAs should be based on the record of recovery.
(D) The auditor should primarily rely on management's verbal assurances.

Ans :

(A) The auditor should not assume system-generated information is correct without evidence.
The text warns auditors, "The auditor should not assume that the system generated information is correct and can be relied upon without evidence." By investigating the suspicious, last-minute credit, the auditor is correctly seeking evidence to validate the "record of recovery" and ensure the account's standard status is genuine and not a superficial entry to avoid NPA classification.

Oct/Nov 2011

106. A bank's management team wants to understand how efficiently its departments are using resources and whether its strategic plans are being effectively implemented across the organization. They are not looking for a financial statement opinion. Which type of audit would be most appropriate for the management to commission to meet this objective?

(A) Statutory Audit
(B) Management Audit
(C) Concurrent Audit
(D) Tax Audit

Ans :

(B) Management Audit
The chapter defines Management Audit as an "assessment of methods and policies of an organisation's management in the administration and the use of resources, tactical and strategic planning." Its objective is to see how far management's goals are fulfilled and to evaluate its efficiency, which directly matches the management team's requirement in this scenario.

May/June 2010

107. An IS auditor uses a Computer-Assisted Audit Technique (CAAT) to scan the entire loan portfolio of a bank and recalculate the interest applied to each of the 500,000 loan accounts for the past year. This procedure is an example of which specific use of CAATs mentioned in the chapter?

(A) Penetration testing

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(D) A Forensic Audit

Ans :

(B) A Systems Audit
The text mentions a specific circular related to IT audits. It states, "RBI vide it's circular dated 30th April 2004 on 'Information Systems Audit - A review of Policies and Practices' had advised Banks to carry out a systems Audit periodically to assess effectiveness of hardware software and operations."

May/June 2006

117. Which of the following areas is covered by the RBI guidelines on Information Systems Audit dated 29th April, 2011?
(A) Business Continuity Planning
(B) Branch profitability analysis
(C) Employee performance appraisal
(D) Capital market investments

Ans :

(A) Business Continuity Planning
The chapter provides a list of nine areas covered by the 2011 RBI guidelines on IS Audit. This list includes IT Governance, Information Security, and notably, "Business Continuity Planning," which is critical for ensuring operational resilience in the face of disruptions. The other options are outside the scope of these specific guidelines.

Oct/Nov 2017

118. According to the guiding principles of IS Audit, in which areas should a continuous IS audit be introduced in a phased manner?
(A) In critical areas
(B) In all branches simultaneously
(C) Only in the head office
(D) Only for foreign exchange transactions

Ans :

(A) In critical areas
The guiding principles from the Master Circular on Audit Systems recommend a pragmatic and risk-based rollout. It states, "Continuous IS audit should be introduced in critical areas in a phased manner." This allows banks to focus their resources on the most important and high-risk systems and processes first.

NODIA

May/June 2008

119. The format of which report, issued by statutory auditors, was revised by an RBI circular dated September 05, 2020?
(A) The main Statutory Audit Report
(B) The Tax Audit Report
(C) The Long Form Audit Report (LFAR)
(D) The NPA Classification Report

Ans :

(C) The Long Form Audit Report (LFAR)
At the end of the section on reports issued by statutory auditors, the text provides a specific update. It states, "RBI has revised the format of Long Form Audit Report vide its circular dated September 05, 2020." This highlights a recent change that auditors need to be aware of.

Oct/Nov 2013

120. What is the primary focus of a Stock and Receivables Audit?
(A) To check on the stock and book debts statements submitted by borrowers.
(B) To check the bank's own inventory of stationery.
(C) To audit the stock of shares held by the bank in its investment portfolio.
(D) To check the cash stock held in the bank's currency chest.

Ans :

(A) To check on the stock and book debts statements submitted by borrowers.
The chapter defines the purpose of this specific audit type clearly. It is conducted "to check on the stock and book debts statements submitted by the borrowers to the bank." This is done to verify the value and existence of the security against which the bank has extended credit, particularly for large borrowers.

May/June 2015

121. Consider the following statements about auditing:
1. The incidental objective of auditing is the detection and prevention of errors and frauds.
2. The auditor's work involves the exercise of judgment.
3. An auditor can check each and every transaction in a large company.
4. An audit provides absolute assurance about the correctness of financial statements.

(A) The Money Measurement Concept
(B) The Going Concern Concept
(C) The Business Entity Concept
(D) The Accrual Concept

Ans :

(C) The Business Entity Concept
The business entity concept is a fundamental accounting principle that treats the business as a separate entity from its owners. Consequently, all business transactions are recorded in the books of the business from its own perspective, not from the owner's personal viewpoint. This is why owner's capital is a liability.

May/June 2013

6. How is the Balance Sheet Equation correctly expressed?
(A) Assets = Capital - Outside Liabilities
(B) Assets = Total Claims = Claims of creditors + Claims of owners
(C) Capital = Assets + Outside Liabilities
(D) Outside Liabilities = Assets + Capital

Ans :

(B) Assets = Total Claims = Claims of creditors + Claims of owners
The balance sheet equation states that the total assets of a business are equal to the total claims against those assets. These claims are divided into two categories: claims of outsiders (creditors/ outside liabilities) and claims of owners (capital/ net worth). Hence, Assets = Outside Liabilities + Capital.

Oct/Nov 2021

7. Which of the following is a correct derivative of the fundamental Balance Sheet Equation?
(A) Capital = Outside Liabilities - Assets
(B) Assets = Capital - Outside Liabilities
(C) Outside Liabilities = Capital - Assets
(D) Capital = Assets - Outside Liabilities

Ans :

(D) Capital = Assets - Outside Liabilities
The primary balance sheet equation is Assets = Outside Liabilities + Capital. By rearranging this equation to solve for Capital, we subtract Outside Liabilities from both sides. This results in the derivative formula: Capital = Assets - Outside Liabilities, which correctly represents the owners' equity or net worth of the business.

May/June 2009

8. If a business has total assets of ₹5,00,000 and its capital is ₹3,50,000, what is the value of its outside liabilities?
(A) ₹1,50,000
(B) ₹8,50,000
(C) ₹3,50,000
(D) ₹5,00,000

Ans :

(A) ₹1,50,000
Using the balance sheet equation, Outside Liabilities = Assets - Capital. Given the assets are ₹5,00,000 and the capital is ₹3,50,000, the outside liabilities can be calculated as ₹ 5,00,000 - ₹ 3,50,000 = ₹ 1,50,000. This amount represents the claims of creditors and other external parties against the business's assets.

Oct/Nov 2006

9. What is the impact on capital if the assets of a business increase while its liabilities remain unchanged?
(A) Capital will decrease.
(B) Capital will remain unchanged.
(C) Capital will increase.
(D) The relationship cannot be determined.

Ans :

(C) Capital will increase.
The capital or owners' claim is directly affected by changes in assets and liabilities. According to the equation Capital = Assets - Liabilities, if assets increase and liabilities do not change, the resulting value of capital must increase. This often happens when the business earns a profit, which increases assets without a corresponding liability increase.

May/June 2018

10. A reduction in the amount of assets or an increase in the amount of liabilities will lead to what effect on capital?
(A) A reduction in the amount of capital.
(B) An increase in the amount of capital.
(C) No change in the amount of capital.
(D) A reduction in assets and an increase in liabilities simultaneously is not possible.

Ans :

(A) A reduction in the amount of capital.
The owner's claim, or capital, is bound to change correspondingly with assets and liabilities. A

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(A) Preparation of the bank's annual budget
(B) Determining Audit Materiality
(C) Assessing Risks Associated with Outsourcing of Activities
(D) Conformity to Basel III framework

Ans :

(A) Preparation of the bank's annual budget
The list of 17 stages in a statutory audit is extensive and covers risk assessment, planning, and execution. It includes determining materiality, assessing outsourcing risks, and checking conformity to Basel III. However, preparing the bank's annual budget is a core management and financial planning function, not a stage of the external audit process.

Oct/Nov 2023

126. The primary objective of a financial audit is to:
(A) enhance the shareholder value.
(B) ensure that the financial statements give a True and Fair view.
(C) detect all errors and frauds.
(D) improve the profitability of the bank.

Ans :

(B) ensure that the financial statements give a True and Fair view.
The fundamental objective of a financial audit is to provide an independent opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework, thereby presenting a 'True and Fair' view of the entity's financial position and performance.

May/June 2016

127. Internal Audit is generally undertaken by whom and for what purpose?
(A) Undertaken by tax experts for tax planning.
(B) Undertaken by the company secretary for statutory compliance.
(C) Undertaken by the bank's own staff to ensure accuracy and correctness of accounts.
(D) Undertaken by auditors approved by RBI for improving profitability.

Ans :

(C) Undertaken by the bank's own staff to ensure accuracy and correctness of accounts.
The chapter states that Internal Audit is generally undertaken by the bank's own staff (and sometimes CA firms) and is "aimed at ensuring the accuracy and correctness of the books of account of banks" to maintain public confidence.

Oct/Nov 2009

128. Which one of the following statements is NOT correct?
(A) Management audit is always conducted by the management of the bank.
(B) Forensic Audit is an examination of financial information for use of evidence in court.
(C) Tax audit is an analysis of the tax returns submitted.
(D) Only large borrower accounts are normally subjected to stock and receivables audit.

Ans :

(A) Management audit is always conducted by the management of the bank.
While management can conduct self-assessments, a Management Audit is an independent assessment of management's effectiveness. It can be conducted by internal auditors or external consultants to provide an objective view. The statement that it is 'always' conducted 'by' the management is incorrect; it is an audit 'of' management.

May/June 2023

129. The Long Form Audit Report (LFAR) is issued by which auditor?
(A) Concurrent Auditor
(B) Internal Auditor
(C) Statutory Auditor
(D) Tax Auditor

NODIA

Ans :

(C) Statutory Auditor
The chapter clearly lists the Long Form Audit Report (LFAR) as one of the "Types of Audit Reports to be issued by Statutory Auditors." It is a key report submitted by the statutory auditor to the bank and RBI, providing detailed information on various aspects of the bank's operations.

Oct/Nov 2018

130. What is the primary difference in focus between a Revenue Audit and a Stock and Receivables Audit?
(A) Revenue audit focuses on the bank's income, while stock audit focuses on borrower's assets.
(B) Revenue audit is for large branches, while stock audit is for small branches.

(B) April 29, 2011
(C) September 18, 2019
(D) January 07, 2021

Ans :

(D) January 07, 2021
The text states that the RBI had introduced the RBIA system on December 27, 2002. It then explicitly mentions, "This was further supplemented vide circular dated January 07, 2021." This later circular provided additional instructions and reinforced the RBIA framework, indicating an evolution and strengthening of the guidelines over time.

Oct/Nov 2015

112. Which of the following is NOT a core component of the RBIA framework mentioned in the chapter?
(A) A well-defined policy for internal audit
(B) Marketing strategies for bank products
(C) Functional independence with sufficient standing
(D) Adequate audit resources with sufficient professional competence

Ans :

(B) Marketing strategies for bank products
The chapter describes the RBIA framework as relying on several pillars. These include a well-defined policy, functional independence, effective communication channels, and adequate, competent resources. Marketing strategies are a business function and are not a component of the internal audit framework, which is focused on control, risk management, and governance.

May/June 2013

113. What is the minimum frequency for the Audit Committee of the Board (ACB) to meet the Head of Internal Audit (HIA) without the presence of senior management?
(A) At least once a year
(B) At least once a half-year
(C) At least once in a quarter
(D) At least once a month

Ans :

(C) At least once in a quarter
To bolster the independence of the internal audit function, the RBI guidelines mandate a private channel of communication. The text specifies that "the ACB shall meet the HIA at least once in a quarter, without the presence of the senior management, including the MD & CEO/WTD," ensuring candid discussion.

Oct/Nov 2021

114. The RBI guidelines on Concurrent Audit were revised via a circular dated:
(A) 27th December 2002
(B) 29th April 2011
(C) 7th January 2021
(D) 18th September 2019

Ans :

(D) 18th September 2019
The text explicitly provides the reference for the revised guidelines on the Concurrent Audit System in Commercial Banks. It states, "RBI has revised the guidelines on Concurrent Audit System in Commercial Banks vide RBI Circular Reference No. DBS.CO.ARS.No.BC.01/08.91.021/2019-20 dated 18th September 2019."

May/June 2024

115. Which of the following is NOT one of the important aspects of Internal Audit listed in the chapter?
(A) Role in determining the bank's lending interest rates
(B) Role in overall governance mechanism of the Banks
(C) Role of Risk-Based Internal Audit in evaluating Risk Management
(D) Auditing and Assurance Standards

Ans :

(A) Role in determining the bank's lending interest rates
The chapter lists several important aspects of Internal Audit, including its role in governance, risk management evaluation, procedures, and adherence to standards. Determining lending interest rates is a commercial and strategic decision made by the bank's management (e.g., ALCO), not a function of the internal audit department.

Oct/Nov 2008

116. The RBI circular dated 30th April 2004 advised banks to periodically carry out which type of audit?
(A) A Concurrent Audit
(B) A Systems Audit
(C) A Management Audit

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CHAPTER 12

Balance Sheet Equation

Oct/Nov 2015

1. According to the fundamental principles of accounting for a business entity, what is the relationship between assets and liabilities?
(A) Assets are always greater than liabilities.
(B) Assets are always equal to liabilities.
(C) Assets are always less than liabilities.
(D) There is no fixed relationship between assets and liabilities.

Ans :

(B) Assets are always equal to liabilities.
For any business entity, an asset is created by taking on a liability of an equal amount. Therefore, at any given point, the total assets of the business will always be equal to its total liabilities, which include claims of both owners and outsiders. This is the foundation of the balance sheet equation.

May/June 2007

2. In the context of a business entity's liabilities, what do the "claims of owners" represent?
(A) The paid-up capital plus the balance of reserves and surplus.
(B) The total amount owed to external creditors and suppliers.
(C) The total value of all assets owned by the business.
(D) The total amount of loans taken from financial institutions.

Ans :

(A) The paid-up capital plus the balance of reserves and surplus.
The liabilities of a business consist of claims from two groups: outsiders and owners. The claims of the owners specifically refer to their investment in the business, which is represented by the paid-up capital, along with any accumulated profits retained in the business, known as reserves and surplus.

Oct/Nov 2019

3. What is another term for the sum of capital and the balance of reserves and surplus in a business entity?
(A) Gross Worth
(B) Total Assets
(C) Net Worth
(D) Outside Liabilities

Ans :

(C) Net Worth
The sum of the owner's capital and the accumulated reserves and surplus is defined as the net worth of the business. It represents the owners' claim against the total assets of the entity. Net worth is a key indicator of the financial health of a business from the perspective of its owners.

May/June 2024

4. From the perspective of a business entity, how is 'net worth' defined?
(A) The claim of the outsiders against the assets of the business.
(B) The total market value of the business's shares.
(C) The total value of tangible assets minus depreciation.
(D) The liability of the business towards its owners.

Ans :

(D) The liability of the business towards its owners.
Based on the separate entity concept in accountancy, the business is treated as distinct from its owners. Therefore, the amount invested by the owners (capital) and the retained earnings (reserves and surplus), collectively known as net worth, are considered a liability of the business towards its owners.

Oct/Nov 2010

5. Which accounting concept mandates that a business and its owners are considered two separate and distinct entities?

NODIA

(C) Revenue audit is statutory, while stock audit is internal.
(D) Revenue audit focuses on expenses, while stock audit focuses on liabilities.

Ans :

(A) Revenue audit focuses on the bank's income, while stock audit focuses on borrower's assets.
Revenue audit is aimed at identifying leakage in the bank's own income (interest and charges). In contrast, a stock and receivables audit is focused on verifying the assets (stock and book debts) of the borrower, which serve as security for the bank's loan. Their focus is distinctly on the bank's income versus the borrower's assets.

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reduction in assets (without a corresponding liability reduction) or an increase in liabilities (without a corresponding asset increase) will both result in a reduction in the amount of capital, as per the equation Capital = Assets - Liabilities.

Oct/Nov 2025

11. Which of the following items would typically be classified under 'Assets' in a balance sheet equation diagram?
(A) Creditors and Bills Payable
(B) Bank Overdraft and Outstanding Expenses
(C) Capital and Reserves and Surplus
(D) Furniture, Machinery, and Building

Ans :

(D) Furniture, Machinery, and Building
Assets represent the resources owned by the business that have future economic value. In a typical balance sheet diagram, items like Cash, Bank, Bills Receivable, Debtors, Stock in trade, Furniture, Machinery, and Building are correctly classified as Assets. Creditors, Bank Overdraft, and Capital are on the Capital + Liabilities side.

May/June 2005

12. Which of the following pairs is INCORRECTLY matched based on the typical structure of a balance sheet?
(A) Asset - Stock in trade
(B) Asset - Bank Overdraft
(C) Liability - Creditors
(D) Liability - Bills payable

Ans :

(B) Asset - Bank Overdraft
A bank overdraft represents an amount owed by the business to the bank, making it a short-term liability. Assets are resources owned by the business, such as stock in trade. Creditors and bills payable are also correctly identified as liabilities, representing amounts owed to suppliers and other parties respectively.

Oct/Nov 2018

13. Identify the item that falls under the 'Capital + Liabilities' side of the balance sheet equation.
(A) Debtors
(B) Bills Receivable
(C) Outstanding expenses
(D) Stock in trade

Ans :

(C) Outstanding expenses
Outstanding expenses are costs that the business has incurred but has not yet paid. This represents an obligation to pay, making it a liability. Therefore, it is correctly placed on the 'Capital + Liabilities' side of the equation. Debtors, bills receivable, and stock in trade are all assets.

May/June 2021

14. What is the initial effect on the balance sheet equation when a person, Mr. R, commences his business with ₹20,000 as capital in cash?
(A) Assets (Cash) increase by ₹20,000; Liabilities (Creditors) increase by ₹20,000.
(B) Liabilities (Loan) increase by ₹20,000; Capital increases by ₹20,000.
(C) Assets remain unchanged; Capital increases by ₹20,000.
(D) Assets (Cash) increase by ₹20,000; Capital increases by ₹20,000.

Ans :

(D) Assets (Cash) increase by ₹20,000; Capital increases by ₹20,000.
When a business is started with cash capital, the business receives cash, which is an asset. Simultaneously, this creates a claim for the owner (Mr. R) against the business, which is recorded as capital. Thus, assets (Cash) increase by ₹20,000 and capital (R's Capital) increases by ₹20,000, keeping the equation in balance.

Oct/Nov 2014

15. Consider the following statements regarding the commencement of a business with ₹20,000 cash.
Statement I : The firm has assets totalling ₹20,000 in the form of cash.
Statement II : The claims against the firm are also ₹20,000 in the form of capital.
(A) Only Statement I is correct.
(B) Only Statement II is correct.
(C) Both Statement I and Statement II are correct.
(D) Both Statement I and Statement II are incorrect.

Ans :

(C) Both Statement I and Statement II are correct.
Starting a business with a cash investment has a dual effect. The business gains an asset, which is the cash itself, valued at ₹20,000. At the same time, it incurs a liability towards the owner for the amount invested, which is recorded as capital

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of ₹20,000. Both statements accurately describe this initial transaction.

May/June 2011

16. Refer to the 'Balance Sheet 1' in the provided text. What does this balance sheet represent?

Liabilities	₹	Assets	₹
R's Capital	20,000	Cash	20,000

(A) The state of the business after purchasing goods on credit.
(B) The financial position immediately after the owner invested initial capital.
(C) The result of selling goods for a profit.
(D) The situation after paying business expenses.

Ans :

(B) The financial position immediately after the owner invested initial capital.
'Balance Sheet 1' shows assets of ₹20,000 in cash and liabilities of ₹20,000 as R's Capital. This perfectly reflects the initial transaction where Mr. R commences his business by introducing ₹20,000 as capital. The cash is the asset owned by the business, and the capital represents the owner's claim against that asset.

Oct/Nov 2005

17. Mr. R starts a business with ₹20,000 in cash. Immediately after this, he considers buying a small office space for ₹15,000 using the business cash. If he proceeds, what will be the state of his total assets?
(A) Total assets will decrease to ₹5,000.
(B) Total assets will remain unchanged at ₹20,000.
(C) Total assets will increase to ₹35,000.
(D) Total assets will increase by ₹15,000.

Ans :

(B) Total assets will remain unchanged at ₹20,000.
The initial total assets are ₹20,000 (cash). Purchasing an office space for cash is a transaction where one asset (cash) is exchanged for another asset (office space). Cash would decrease by ₹15,000, but a new asset (office space) of ₹15,000 would be acquired. The total value of assets remains constant at ₹20,000.

May/June 2019

18. When the business purchased machinery for ₹1,000, what was the net effect on the total assets of the firm?
(A) Total assets remained unchanged.
(B) Total assets increased by ₹1,000.
(C) Total assets decreased by ₹1,000.
(D) Total assets increased by ₹2,000.

Ans :

(A) Total assets remained unchanged.
The purchase of machinery for cash involves an exchange of one asset for another. The cash balance decreased by ₹1,000, while a new asset, machinery, was acquired for ₹1,000. The composition of assets changed, but the total value of assets remained the same (₹20,000), thereby keeping the balance sheet equation in equilibrium.

Oct/Nov 2012

19. After the purchase of machinery for ₹1,000, what were the balances of Cash and Machinery accounts respectively?
(A) Cash ₹20,000; Machinery ₹1,000
(B) Cash ₹21,000; Machinery ₹1,000
(C) Cash ₹19,000; Machinery ₹1,000
(D) Cash ₹19,000; Machinery ₹0

Ans :

(C) Cash ₹19,000; Machinery ₹1,000
The business started with ₹20,000 in cash. When it paid ₹1,000 for machinery, the cash balance was reduced to ₹ 20,000 - ₹ 1,000 = ₹ 19,000. Simultaneously, a new asset account, Machinery, was created with a balance of ₹1,000. The total assets remained ₹ 19,000 + ₹ 1,000 = ₹ 20,000.

May/June 2012

20. Identify the correct statement regarding the transaction of purchasing machinery for ₹1,000 cash.
(A) It changed the composition of assets but left total assets unchanged.
(B) It increased total assets and total liabilities.
(C) It decreased total assets and capital.
(D) It increased machinery and increased capital.

Ans :

(A) It changed the composition of assets but left total assets unchanged.
This transaction is an exchange of one asset (cash) for another (machinery). The amount of cash in hand was lowered, but a new asset of equal value was acquired. This alters the mix of assets the business holds but does not change the

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total value of assets or the total of liabilities and capital.

Oct/Nov 2007

21. Examine 'Balance Sheet 2' from the text.

Liabilities	₹	Assets	₹
R's Capital	20,000	Cash (20,000 - 1,000)	19,000
		Machinery (0 + 1,000)	1,000
Total	**20,000**	**Total**	**20,000**

What transaction led to this financial position?
(A) Starting a business with ₹19,000 cash and ₹1,000 machinery.
(B) Selling machinery for ₹1,000 in cash.
(C) Taking a loan of ₹1,000 to buy machinery.
(D) Purchasing a machinery of ₹1,000 for cash.

Ans :

(D) Purchasing a machinery of ₹1,000 for cash.
'Balance Sheet 2' shows that cash has decreased from ₹20,000 to ₹19,000, and a new asset, machinery, of ₹1,000 has been added. This is the exact result of using ₹1,000 cash to purchase machinery. Total assets and total capital plus liabilities both remain at ₹20,000.

May/June 2025

22. What is the effect of the business purchasing goods for ₹2,000 for cash?
(A) Total assets increase by ₹2,000.
(B) Total assets remain unchanged.
(C) Total assets decrease by ₹2,000.
(D) Capital increases by ₹2,000.

Ans :

(B) Total assets remain unchanged.
Similar to the purchase of machinery, buying goods (stock) for cash is an exchange of one asset for another. The asset 'Cash' decreases by ₹2,000, while the asset 'Stock of goods' increases by ₹2,000. This changes the composition of assets but does not alter the total value of assets.

Oct/Nov 2020

23. After purchasing machinery for ₹1,000 and then goods for ₹2,000, both for cash, what is the final cash balance of the business?
(A) ₹20,000
(B) ₹19,000
(C) ₹17,000
(D) ₹18,000

Ans :

(C) ₹17,000
The business started with ₹20,000 cash. The first transaction (machinery purchase) reduced it to ₹19,000 (₹ 20,000 - ₹ 1,000). The second transaction (goods purchase) further reduced it by ₹2,000. The final cash balance is ₹ 19,000 - ₹ 2,000 = ₹ 17,000, as reflected in 'Balance Sheet 3'.

May/June 2006

24. Which of the following statements is INCORRECT regarding the state of the business after it has purchased goods for ₹2,000 cash (Transaction 3)?
(A) The cash in hand is lower by ₹2,000 compared to the previous state.
(B) A new asset (stock of goods) has been acquired.
(C) The total assets have remained unchanged at ₹20,000.
(D) The owner's capital has decreased to ₹18,000.

Ans :

(D) The owner's capital has decreased to ₹18,000.
Purchasing goods for cash is an asset conversion transaction. It does not involve any expense or income, nor does it affect liabilities. Therefore, the owner's capital remains unchanged at ₹20,000. The cash decreased, a new asset (goods) was created, and total assets stayed the same.

Oct/Nov 2011

25. What is the impact on the accounting equation when a business purchases goods for ₹5,000 on credit?
(A) Assets increase by ₹5,000, and Capital increases by ₹5,000.
(B) Assets decrease by ₹5,000, and Liabilities decrease by ₹5,000.
(C) Assets increase by ₹5,000, and Liabilities increase by ₹5,000.
(D) There is no change in the total of the balance sheet.

Ans :

(C) Assets increase by ₹5,000, and Liabilities increase by ₹5,000.
When goods are purchased on credit, the business acquires an asset (stock of goods), causing total assets to increase. Since the payment is not made immediately, an obligation to pay the supplier is created. This obligation is a liability (creditor),

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(B) Purchase of goods for cash.
When goods are purchased for cash, one asset (cash) is exchanged for another asset (goods) of equal value. For example, in Transaction 3, cash decreased by ₹2,000 while goods increased by ₹2,000. The total assets remained unchanged at ₹20,000. This is a pure asset conversion transaction.

Oct/Nov 2014

57. Which transaction resulted in an increase in both total assets and total liabilities?
(A) Commencing business with capital.
(B) Purchasing machinery for cash.
(C) Selling goods on credit for a profit.
(D) Purchasing goods on credit.

Ans :

(D) Purchasing goods on credit.
Transaction 4, the purchase of goods for ₹5,000 on credit, increased the asset 'Goods' by ₹5,000 and created a liability 'Creditor' for ₹5,000. This caused the total of both the assets side and the liabilities side of the balance sheet to increase from ₹20,000 to ₹25,000.

May/June 2011

58. Which transaction resulted in a decrease in an asset and a corresponding decrease in the owner's equity (surplus)?
(A) Payment of rent and salaries.
(B) Purchase of goods for cash.
(C) Purchase of goods on credit.
(D) Sale of goods on credit.

Ans :

(A) Payment of rent and salaries.
Transaction 6 involved paying ₹1,000 for expenses. This reduced the asset 'Cash' by ₹1,000. Since these were expenses and did not create an asset, the cost was borne by the owner, leading to a reduction in the 'Reserves & Surplus' account by ₹1,000, thus decreasing the owner's equity.

Oct/Nov 2005

59. Imagine Mr. R's business is at the stage of Balance Sheet 2 (Total assets ₹20,000). He then decides to take a bank loan of ₹10,000, which is credited to his business bank account. What is the effect on the accounting equation?
(A) Assets increase by ₹10,000; Capital increases by ₹10,000.
(B) Assets remain unchanged; Capital increases by ₹10,000.
(C) Assets increase by ₹10,000; Outside Liabilities increase by ₹10,000.
(D) Assets increase by ₹10,000; Outside Liabilities decrease by ₹10,000.

Ans :

(C) Assets increase by ₹10,000; Outside Liabilities increase by ₹10,000.
Taking a bank loan brings cash (or bank balance, an asset) into the business, so total assets increase by ₹10,000. Simultaneously, it creates an obligation to repay the bank, which is an outside liability. Therefore, outside liabilities also increase by ₹10,000, and the balance sheet total would become ₹30,000.

May/June 2019

60. Match the transaction with its effect on the accounting equation.

List I (Transaction)		**List II (Effect)**	
P.	Purchase of asset for cash	1.	Increase in Asset, Increase in Liability
Q.	Purchase of asset on credit	2.	Decrease in Asset, Decrease in Liability
R.	Repayment of loan	3.	Increase in one Asset, Decrease in another Asset
S.	Sale of goods on credit (at a profit)	4.	Increase in Assets, Increase in Owner's Equity

(A) P-3, Q-1, R-2, S-4
(B) P-1, Q-3, R-4, S-2
(C) P-3, Q-2, R-1, S-4
(D) P-4, Q-1, R-2, S-3

Ans :

(A) P-3, Q-1, R-2, S-4
P: Purchase for cash is an asset swap (e.g., cash for machinery). Q: Purchase on credit increases an asset and a liability (creditor). R: Repaying a loan reduces an asset (cash) and a liability (loan). S: Sale on credit at a profit increases assets (debtor) and owner's equity (surplus).

Oct/Nov 2012

61. If a company's total assets are ₹12,00,000 and its net worth is ₹7,00,000, what is the value of its outside liabilities?

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(R's Capital) remains at its original ₹20,000. A new outside liability, 'Creditor', has been added with a value of ₹5,000. The sum of these two components gives the total liabilities of ₹25,000.

Oct/Nov 2023

31. When the business sells goods on credit for ₹5,000, with the cost of these goods being ₹3,000, what new asset is created?
(A) Cash of ₹5,000
(B) Stock of ₹3,000
(C) Surplus of ₹2,000
(D) Debtor of ₹5,000

Ans :

(D) Debtor of ₹5,000
A sale on credit means the business has a right to receive money from the customer in the future. This right to receive money is an asset known as a 'Debtor'. The value of the debtor is the selling price of the goods, which is ₹5,000 in this case.

May/June 2017

32. In the transaction of selling goods for ₹5,000 (cost ₹3,000) on credit, what is the change in the 'Goods' (stock) account?
(A) It increases by ₹5,000
(B) It reduces by ₹3,000
(C) It increases by ₹3,000
(D) It reduces by ₹5,000

Ans :

(B) It reduces by ₹3,000
The 'Goods' or stock-in-trade account is always maintained at its cost price. When goods are sold, the stock account must be reduced by the cost of the goods that have been sold. In this transaction, the cost of the goods sold was ₹3,000, so the stock account is reduced by this amount.

Oct/Nov 2013

33. What is the net increase in total assets resulting from selling goods on credit for ₹5,000 that cost ₹3,000?
(A) ₹5,000
(B) ₹3,000
(C) ₹2,000
(D) ₹8,000

Ans :

(C) ₹2,000
This transaction has two effects on assets: a new asset, 'Debtor', is created for ₹5,000, and an existing asset, 'Goods', is reduced by ₹3,000. The net change in total assets is the increase minus the decrease, which is ₹ 5,000 - ₹ 3,000 = ₹ 2,000.

May/June 2010

34. The net increase in assets of ₹2,000 from the credit sale (selling price ₹5,000, cost ₹3,000) is recognized as what on the liabilities side?
(A) A new loan
(B) An increase in Creditors
(C) A reduction in Capital
(D) A surplus belonging to the owner

Ans :

(D) A surplus belonging to the owner
The difference between the selling price (₹5,000) and the cost of goods sold (₹3,000) is the profit, or surplus, from the transaction. This profit of ₹2,000 belongs to the owner of the business. It increases the owner's net worth and is shown as 'Reserves & Surplus' on the liabilities side.

Oct/Nov 2009

35. After the credit sale transaction (selling goods for ₹5,000, cost ₹3,000), what is the new net worth of the owner?
(A) ₹22,000
(B) ₹20,000
(C) ₹18,000
(D) ₹25,000

Ans :

(A) ₹22,000
The owner's initial net worth was the capital of ₹20,000. The profit (surplus) of ₹2,000 (₹ 5,000 - ₹ 3,000) from the sale belongs to the owner. This surplus is added to the initial capital to determine the new net worth. Therefore, the new net worth is ₹20,000 (Capital) + ₹2,000 (Surplus) = ₹22,000.

May/June 2023

36. Following the credit sale, Mr. R's business has the financial position shown in Balance Sheet 5. If the debtor immediately pays ₹4,000 of the ₹5,000 owed, what would be the impact on the balance sheet?
(A) Cash increases by ₹4,000, Surplus increases by ₹4,000.
(B) Cash increases by ₹4,000, Debtor decreases by ₹4,000, Total Assets remain unchanged.
(C) Cash increases by ₹4,000, Debtor decreases by ₹5,000.
(D) Total Assets increase by ₹4,000.

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(C) Debtor
(D) Expense

Ans :

(B) Depreciation
The keywords section at the end of the chapter lists "Capital; Liability; Assets; Revenue/ Income; Expense; Debtor; Creditor". The term 'Depreciation', while an important accounting concept, is not mentioned in this specific list or discussed in the provided text, making it the correct answer.

Oct/Nov 2010

47. According to the "Check Your Progress" section, what is the effect of converting a loan into equity?
(A) Change in both assets and liabilities.
(B) Change in total assets only.
(C) Change in total liabilities only.
(D) Change in liabilities but total liabilities remain the same.

Ans :

(D) Change in liabilities but total liabilities remain the same.
Converting a loan (an outside liability) into equity (owner's liability/capital) is a reclassification within the 'Capital + Liabilities' side of the balance sheet. One liability (loan) decreases while another liability (capital) increases by the same amount. Total liabilities and total assets remain unchanged.

May/June 2013

48. What is the impact of purchasing fixed assets on credit, as per the "Check Your Progress" questions?
(A) Change in both assets and liabilities.
(B) Change in total assets only.
(C) Change in total liabilities only.
(D) Change in liabilities but total liabilities remain the same.

Ans :

(A) Change in both assets and liabilities.
When a fixed asset is purchased on credit, the business acquires an asset, which increases the total assets. Simultaneously, an obligation to pay the supplier is created, which increases the total outside liabilities (creditors). Therefore, both total assets and total liabilities increase by the same amount.

Oct/Nov 2021

49. Mr. R's business is in the state of Balance Sheet 6 (Total Assets/Liabilities ₹26,000). He now decides to repay the ₹5,000 creditor in full using business cash. What is the impact of this transaction?
(A) Assets decrease by ₹5,000 and Capital decreases by ₹5,000.
(B) There is no change in total assets or total liabilities.
(C) Assets decrease by ₹5,000 and Liabilities decrease by ₹5,000.
(D) Assets increase by ₹5,000 and Liabilities increase by ₹5,000.

Ans :

(C) Assets decrease by ₹5,000 and Liabilities decrease by ₹5,000.
Repaying a creditor involves a cash outflow, so the asset 'Cash' will decrease by ₹5,000. This payment settles the obligation to the supplier, so the liability 'Creditor' will also decrease by ₹5,000. Both sides of the balance sheet equation decrease equally, and the new total will be ₹21,000.

May/June 2009

50. What does the "Check Your Progress" section indicate as the result of a sale of goods on credit?
(A) Change in assets but total assets remain the same.
(B) Change in both assets and liabilities.
(C) Change in total assets only.
(D) Change in total liabilities only.

Ans :

(A) Change in assets but total assets remain the same.
This question from the text assumes a sale at cost price for simplicity. In such a case, one asset (goods) decreases and another asset (debtors) increases by the same amount. This changes the composition of assets but keeps the total asset value the same, similar to a cash purchase of an asset.

Oct/Nov 2006

51. Which of the following statements about the business entity concept is correct?
1. The business is treated as separate from its owners.
2. Transactions are recorded from the owner's point of view.
3. The owner's capital is considered a liability of the business.

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(B) Total ₹26,000; composed of Cash, Machinery, and Goods only.
(C) Total ₹25,000; composed of Cash, Machinery, Goods, and Debtor.
(D) Total ₹26,000; composed of Cash, Machinery, Goods, and Debtor.

Ans :

(D) Total ₹26,000; composed of Cash, Machinery, Goods, and Debtor.
The asset side of 'Balance Sheet 6' clearly lists four components: Cash at ₹16,000, Machinery at ₹1,000, Goods at ₹4,000, and Debtor at ₹5,000. The sum of these individual asset values is ₹ 16,000 + ₹ 1,000 + ₹ 4,000 + ₹ 5,000, which correctly totals ₹26,000.

May/June 2015

42. In the final state shown in 'Balance Sheet 6', what is the total amount contributed by the owner versus the amount obtained from outsiders?
(A) Owner: ₹26,000; Outsiders: ₹0
(B) Owner: ₹21,000; Outsiders: ₹5,000
(C) Owner: ₹20,000; Outsiders: ₹6,000
(D) Owner: ₹5,000; Outsiders: ₹21,000

Ans :

(B) Owner: ₹21,000; Outsiders: ₹5,000
The owner's contribution, or net worth, is the sum of Capital (₹20,000) and Reserves & Surplus (₹1,000), which totals ₹21,000. The amount obtained from outsiders is represented by the 'Creditor' account, which has a balance of ₹5,000. These are the two sources of funds for the business.

Oct/Nov 2015

43. What fundamental conclusion is drawn from the series of transactions presented for Mr. R's business?
(A) Total assets will always be greater than total liabilities.
(B) Owner's capital remains fixed regardless of business operations.
(C) Every transaction has a double effect, keeping the balance sheet in equilibrium.
(D) A business can only grow by taking on more debt.

Ans :

(C) Every transaction has a double effect, keeping the balance sheet in equilibrium.
The series of six transactions demonstrates that each event has a dual impact on the balance sheet. For instance, an increase in an asset might correspond to a decrease in another asset or an increase in a liability or capital, ensuring that the equation 'Assets = Liabilities + Capital' always holds true.

May/June 2007

44. The left-hand side (Liabilities + Capital) of the balance sheet shows the sources of funds, while the right-hand side (Assets) shows what?
(A) The profits earned by the business.
(B) The expenses incurred by the business.
(C) The total debt of the business.
(D) How the funds have been invested by the business.

Ans :

(D) How the funds have been invested by the business.
The balance sheet presents a dual perspective. The Capital and Liabilities side details where the business has obtained its funds from (owners and outsiders). The Assets side shows the application or use of these funds, detailing how they have been invested in various resources like cash, machinery, and stock.

Oct/Nov 2019

45. Which of the following equations correctly represents the relationship between Assets, Net Worth, and Creditors as summarized at the end of the chapter?
(A) Assets = Net Worth + Creditors
(B) Assets = Net Worth - Creditors
(C) Net Worth = Assets + Creditors
(D) Creditors = Assets + Net Worth

Ans :

(A) Assets = Net Worth + Creditors
The summary explicitly states the final form of the equation as 'Assets = Net worth + Creditors'. This is a restatement of the primary equation, where 'Net Worth' represents the claims of owners (Capital + Reserves) and 'Creditors' represents the claims of outsiders (Outside Liabilities).

May/June 2024

46. Which of the following is NOT listed as a keyword in the chapter?
(A) Capital
(B) Depreciation

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Ans :

(B) Cash increases by ₹4,000, Debtor decreases by ₹4,000, Total Assets remain unchanged.
The collection of cash from a debtor is a conversion of one asset ('Debtor') into another asset ('Cash'). Cash would increase by the amount received (₹4,000), and the Debtor's balance would decrease by the same amount. This transaction does not affect total assets, liabilities, or owner's equity.

Oct/Nov 2024

37. What is the total of the assets side in 'Balance Sheet 5'?
(A) ₹25,000
(B) ₹20,000
(C) ₹22,000
(D) ₹27,000

Ans :

(D) ₹27,000
According to 'Balance Sheet 5', the assets are: Cash (₹17,000), Machinery (₹1,000), Goods (₹4,000), and Debtor (₹5,000). The sum of these assets is ₹ 17,000 + ₹ 1,000 + ₹ 4,000 + ₹ 5,000 = ₹ 27,000. This matches the total on the liabilities side (Capital ₹20,000 + Surplus ₹2,000 + Creditor ₹5,000).

May/June 2014

38. What is the effect on the accounting equation when the business pays ₹500 for rent and ₹500 for salaries?
(A) Assets (Cash) decrease by ₹1,000, and Capital (Surplus) decreases by ₹1,000.
(B) Assets (Cash) decrease by ₹1,000, and Liabilities (Creditors) decrease by ₹1,000.
(C) Assets (Cash) decrease by ₹1,000, and a new asset (Prepaid Expenses) is created for ₹1,000.
(D) Assets (Cash) increase by ₹1,000, and Capital (Surplus) increases by ₹1,000.

Ans :

(A) Assets (Cash) decrease by ₹1,000, and Capital (Surplus) decreases by ₹1,000.
Paying expenses like rent and salaries uses up cash, so the 'Cash' asset decreases by the total amount paid (₹ 500 + ₹ 500 = ₹ 1,000). Since these payments do not create any new asset, they are treated as expenses. Expenses reduce the owner's equity, so the 'Surplus' account is decreased by ₹1,000.

Oct/Nov 2016

39. After paying ₹1,000 for rent and salaries, what is the new balance of the 'Reserves & Surplus' account?
(A) ₹2,000
(B) ₹3,000
(C) ₹1,000
(D) ₹0

Ans :

(C) ₹1,000
Before this transaction (in Balance Sheet 5), the 'Reserves & Surplus' account had a balance of ₹2,000, which was the profit from the credit sale. The payment of expenses totaling ₹1,000 is borne by the owner and thus reduces this surplus. The new balance is ₹ 2,000 - ₹ 1,000 = ₹ 1,000.

May/June 2020

40. Consider the payment of ₹1,000 in expenses. Why is there no new asset created to show for this payment?
(A) Because the benefits of rent and salaries have been consumed.
(B) Because the payment was made in cash.
(C) Because the amount was too small to be recorded as an asset.
(D) Because it was an illegal payment.

Ans :

(A) Because the benefits of rent and salaries have been consumed.
Expenses are costs incurred for services or benefits that have been used up in the process of generating revenue. Unlike the purchase of machinery or goods which provide future economic benefits, the benefits from rent for a past period and salaries for work already done have been consumed, so no asset is created.

Oct/Nov 2022

41. Refer to 'Balance Sheet 6'. What is the total value of assets and how is it composed?

Assets	**₹**
Cash (17,000 - 1,000)	16,000
Machinery (1,000 + 0)	1,000
Goods (4,000 - 0)	4,000
Debtor (5,000 + 0)	5,000
Total	26,000

(A) Total ₹27,000; composed of Cash, Machinery, Goods, and Creditors.

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(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(C) 1 and 3 only
The business entity concept posits that the business and its owners are distinct entities. Consequently, transactions are recorded from the business's perspective, not the owner's. This is why the capital contributed by the owner is treated as a liability of the business towards the owner, making statements 1 and 3 correct.

May/June 2018

52. What constitutes the 'Total Claims' against a business's assets?
(A) Claims of owners only
(B) Claims of creditors only
(C) Claims of government and tax authorities only
(D) Claims of creditors and claims of owners

Ans :

(D) Claims of creditors and claims of owners
The total assets of a business are financed by funds from two main sources: the owners and outsiders. The claims of these two groups on the assets are known as 'Total Claims'. These consist of the claims of creditors (outside liabilities) and the claims of owners (capital or net worth).

Oct/Nov 2025

53. If a firm's assets increase by ₹50,000 and its outside liabilities decrease by ₹20,000, what is the change in its capital?
(A) Decrease by ₹70,000
(B) Increase by ₹30,000
(C) Increase by ₹70,000
(D) Decrease by ₹30,000

Ans :

(C) Increase by ₹70,000
The equation is Capital = Assets - Outside Liabilities. The change in capital is the change in assets minus the change in liabilities. Change in Capital = (+₹ 50,000) - (-₹ 20,000) = ₹ 50,000 + ₹ 20,000 = +₹ 70,000. Thus, the capital increases by ₹70,000, reflecting an increase in the owner's claim on the business.

May/June 2005

54. Identify the incorrect pair from the following classifications.
(A) Building: Asset
(B) Creditors: Liability
(C) Bills Receivable: Asset
(D) Reserves and Surplus: Asset

Ans :

(D) Reserves and Surplus: Asset
'Reserves and Surplus' represent the accumulated profits of the business that have been retained and not distributed to the owners. This amount is part of the owner's claim (Net Worth) against the business and is therefore classified under the 'Capital + Liabilities' side of the balance sheet, not as an asset.

Oct/Nov 2018

55. The text states: "The liabilities consist of claims of owners and claims of outsiders." In the context of Balance Sheet 6, what are the respective values for 'claims of owners' and 'claims of outsiders'?
(A) Claims of owners: ₹21,000; Claims of outsiders: ₹5,000
(B) Claims of owners: ₹20,000; Claims of outsiders: ₹6,000
(C) Claims of owners: ₹26,000; Claims of outsiders: ₹0
(D) Claims of owners: ₹1,000; Claims of outsiders: ₹25,000

Ans :

(A) Claims of owners: ₹21,000; Claims of outsiders: ₹5,000
The claims of owners (Net Worth) are the sum of R's Capital (₹20,000) and Reserves & Surplus (₹1,000), which equals ₹21,000. The claims of outsiders are represented by the 'Creditor' account, which has a balance of ₹5,000. These values correctly represent the sources of funds for the business at that stage.

May/June 2021

56. Which transaction described in the chapter leads to a change in the composition of assets without changing the total value of assets?
(A) Purchase of goods on credit.
(B) Purchase of goods for cash.
(C) Sale of goods on credit for a profit.
(D) Payment of salaries.

Ans :

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causing total liabilities to increase by the same amount.

May/June 2016

26. Mr. R's business, which currently has assets of ₹20,000 (Cash ₹17,000, Machinery ₹1,000, Goods ₹2,000) and Capital of ₹20,000, now purchases additional goods worth ₹5,000 on credit. What will be the new total of the balance sheet?
(A) ₹20,000
(B) ₹25,000
(C) ₹30,000
(D) ₹15,000

Ans :

(B) ₹25,000
The purchase on credit increases the asset 'Goods' by ₹5,000, making the total assets ₹ 20,000 + ₹ 5,000 = ₹ 25,000. Simultaneously, a liability 'Creditor' of ₹5,000 is created. The new total of the liabilities side becomes Capital (₹20,000) + Creditor (₹5,000) = ₹25,000. The balance sheet now totals ₹25,000.

Oct/Nov 2008

27. After the business purchased goods for ₹5,000 on credit, what was the balance of the Creditor account?
(A) ₹20,000
(B) ₹0
(C) ₹25,000
(D) ₹5,000

Ans :

(D) ₹5,000
Before this transaction, there were no outside liabilities, so the Creditor balance was zero. By purchasing goods on credit, the business incurred a liability to pay the supplier. This created a creditor account with a balance of ₹5,000, representing the amount payable to the supplier of goods.

May/June 2022

28. Following the credit purchase of goods worth ₹5,000, what is the total value of goods (stock) held by the business?
(A) ₹7,000
(B) ₹2,000
(C) ₹5,000
(D) ₹3,000

Ans :

(A) ₹7,000
Before this transaction, the business had goods worth ₹2,000 (from the cash purchase). The credit purchase added another ₹5,000 worth of goods. Therefore, the total value of goods held by the business is the sum of the two purchases, which is ₹ 2,000 + ₹ 5,000 = ₹ 7,000.

Oct/Nov 2017

29. **Assertion (A) :** The purchase of goods on credit increases the total size of the balance sheet.
Reason (R) : This transaction results in an increase in an asset (stock) and a simultaneous increase in a liability (creditor).
(A) Both A and R are true, and R is the correct explanation of A.
(B) Both A and R are true, but R is not the correct explanation of A.
(C) A is true, but R is false.
(D) A is false, but R is true.

Ans :

(A) Both A and R are true, and R is the correct explanation of A.
Purchasing on credit brings a new asset (stock) into the business and creates a new liability (creditor) of the same value. Since both the asset side and the liability side of the balance sheet increase, the total size of the balance sheet grows, proving the assertion. The reason correctly explains this mechanism.

May/June 2008

30. Based on 'Balance Sheet 4', what are the components and total of the liabilities side?

Liabilities	**₹**
R's Capital	20,000
Creditor (0 + 5,000)	5,000
Total	25,000

(A) R's Capital ₹20,000, Creditor ₹5,000; Total ₹25,000.
(B) R's Capital ₹25,000; Total ₹25,000.
(C) R's Capital ₹20,000, Loan ₹5,000; Total ₹25,000.
(D) Creditor ₹25,000; Total ₹25,000.

Ans :

(A) R's Capital ₹20,000, Creditor ₹5,000; Total ₹25,000.
The liabilities side of 'Balance Sheet 4' clearly shows two components. The owner's claim

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(A) ₹19,00,000
(B) ₹7,00,000
(C) Cannot be determined.
(D) ₹5,00,000

Ans :

(D) ₹5,00,000
The fundamental accounting equation is Assets = Net Worth + Outside Liabilities. Rearranging this to find outside liabilities gives: Outside Liabilities = Assets - Net Worth. Plugging in the given values, we get ₹ 12,00,000 - ₹ 7,00,000 = ₹ 5,00,000. This represents the claims of external parties against the company's assets.

May/June 2012

62. Which of the following correctly describes the dual effect of a transaction?
(A) Every transaction affects only the asset side of the balance sheet.
(B) A change in an asset will have a corresponding effect on liabilities or capital or another asset.
(C) Every transaction affects only the liability side of the balance sheet.
(D) A transaction can increase an asset without any other change.

Ans :

(B) A change in an asset will have a corresponding effect on liabilities or capital or another asset.
The principle of double-entry accounting, reflected in the balance sheet equation, is that every transaction has a dual effect. Any change on one side of the equation must be matched by an equal change, ensuring the balance sheet always remains in balance. This corresponding effect maintains the fundamental equality.

Oct/Nov 2007

63. From the examples provided, which of the following is an example of an outside liability?
(A) R's Capital
(B) Reserves & Surplus
(C) Creditor
(D) Debtor

Ans :

(C) Creditor
Outside liabilities are claims against the business's assets by external parties. In the given examples, the 'Creditor' account represents the amount owed to a supplier for goods purchased on credit, making it an outside liability. R's Capital and Reserves & Surplus are owner's claims, and Debtor is an asset.

May/June 2025

64. What is the primary purpose of the Balance Sheet Equation?
(A) To calculate the annual profit or loss of a business.
(B) To list all the expenses incurred by the business during a period.
(C) To determine the cash flow from operating activities.
(D) To show that the total assets of a business are always equal to the total claims against it.

Ans :

(D) To show that the total assets of a business are always equal to the total claims against it.
The balance sheet equation, Assets = Liabilities + Capital, is the structural foundation of the balance sheet itself. Its primary purpose is to represent the fundamental accounting truth that a business's resources (assets) are always equal in value to the claims against those resources by both outsiders (liabilities) and owners (capital).

Oct/Nov 2020

65. If a business's capital is ₹1,00,000, and its outside liabilities are ₹40,000, what must be the value of its total assets?
(A) ₹1,40,000
(B) ₹60,000
(C) ₹40,000
(D) ₹1,00,000

Ans :

(A) ₹1,40,000
According to the balance sheet equation, Assets = Capital + Outside Liabilities. Given the capital is ₹1,00,000 and outside liabilities are ₹40,000, the total assets must be the sum of these two figures. Therefore, Total Assets = ₹ 1,00,000 + ₹ 40,000 = ₹ 1,40,000, ensuring the equation remains in balance.

May/June 2006

66. A reduction in the amount of capital can be caused by:
I. A reduction in assets.
II. An increase in liabilities.
III. An increase in assets.
(A) I only
(B) II only

When the owner introduces an additional ₹1,00,000, this amount is added directly to the existing capital. The new capital value becomes ₹ 6,00,000 + ₹ 1,00,000 = ₹ 7,00,000.

Oct/Nov 2020

107. What is the primary difference between a 'debtor' and a 'creditor' in accounting?
(A) A debtor is a liability, while a creditor is an asset.
(B) Both are assets of the business.
(C) Both are liabilities of the business.
(D) A debtor is an asset, while a creditor is a liability.

Ans :

(D) A debtor is an asset, while a creditor is a liability.
A debtor represents money owed to the business by a customer, making it a resource or an asset. A creditor represents money owed by the business to a supplier or lender, making it an obligation or a liability. They represent opposite sides of a credit transaction.

May/June 2006

108. The term 'double effect' as used in the chapter's conclusion means that every transaction:
(A) affects at least two different accounts, keeping the equation in balance.
(B) must be recorded twice in the journal.
(C) doubles the value of the business.
(D) involves both a cash and a credit component.

Ans :

(A) affects at least two different accounts, keeping the equation in balance.
The concept of 'double effect' or duality is the cornerstone of the accounting equation. It means that every single business transaction has at least two impacts on the financial position. These impacts are equal and opposite in a way that always maintains the equality of Assets = Liabilities + Capital.

Oct/Nov 2011

109. If a business's total assets decrease by ₹30,000 and its capital decreases by ₹10,000, what must have been the change in its outside liabilities?
(A) Increased by ₹20,000
(B) Decreased by ₹40,000
(C) Decreased by ₹20,000
(D) Increased by ₹40,000

Ans :

(C) Decreased by ₹20,000
The equation is Assets = Liabilities + Capital. The change in assets must equal the sum of changes in liabilities and capital. So, -₹ 30,000 = Change in Liabilities + (-₹ 10,000). Solving for the change in liabilities gives -₹ 30,000 + ₹ 10,000 = -₹ 20,000. Thus, liabilities must have decreased by ₹20,000.

May/June 2016

110. Which of the following groups of accounts all belong on the Asset side of the balance sheet?
(A) Building, Bills Receivable, Debtors
(B) Cash, Debtors, Creditors
(C) Machinery, Stock in trade, Bank Overdraft
(D) R's Capital, Furniture, Bank

Ans :

(A) Building, Bills Receivable, Debtors
Building is a fixed asset. Bills Receivable is a current asset representing money to be received. Debtors are also current assets representing money owed by customers. All three are resources owned by the business. The other options contain liability or equity accounts like Creditors, Bank Overdraft, and R's Capital.

Oct/Nov 2008

111. Consider the following statements:
I. Every transaction affects the Balance Sheet.
II. Total Assets are always equal to Net Worth.
III. The claim of the owners is also called Capital.
Which of the above statements is/are correct?
(A) I and II only
(B) III only
(C) I, II, and III
(D) I and III only

Ans :

(D) I and III only
Every transaction has a dual effect and thus impacts the balance sheet. The claim of the owners is indeed called Capital or Net Worth. However, Total Assets are equal to Net Worth plus Outside Liabilities, not just Net Worth alone, unless the business has zero outside liabilities.

May/June 2022

112. The text states: "For a business entity, net worth is the liability of the business towards the owners." This statement is a direct consequence of which accounting concept?

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the funds have been invested by the business.
(A) Only Statement I is correct.
(B) Only Statement II is correct.
(C) Both Statement I and Statement II are correct.
(D) Both Statement I and Statement II are incorrect.

Ans :

(C) Both Statement I and Statement II are correct.
The balance sheet provides a two-sided view of the business's financial position. The liabilities and capital side (traditionally the left side) details the sources of funds, i.e., from owners and outsiders. The asset side (traditionally the right side) details the uses or investments of those funds in various resources.

May/June 2008

72. Mr. R's business is at the stage of Balance Sheet 4 (Total ₹25,000). The owner, Mr. R, withdraws ₹2,000 cash for his personal use. What is the impact on the balance sheet equation?
(A) Assets (Cash) decrease by ₹2,000; Liabilities (Creditors) decrease by ₹2,000.
(B) Assets (Cash) decrease by ₹2,000; Capital (R's Capital) decreases by ₹2,000.
(C) Assets (Cash) increase by ₹2,000; Capital (R's Capital) increases by ₹2,000.
(D) This transaction does not affect the balance sheet.

Ans :

(B) Assets (Cash) decrease by ₹2,000; Capital (R's Capital) decreases by ₹2,000.
When the owner withdraws cash for personal use (drawings), the business's cash asset decreases. This withdrawal reduces the owner's claim on the business. Therefore, both the asset 'Cash' and 'R's Capital' will decrease by ₹2,000. The new balance sheet total would be ₹23,000.

Oct/Nov 2023

73. Which of the following will result in an increase in owner's equity?
(A) Purchase of an asset on credit.
(B) Payment of a liability.
(C) Introduction of fresh capital by the owner.
(D) Withdrawal of cash by the owner for personal use.

Ans :

(C) Introduction of fresh capital by the owner.
Owner's equity (or net worth) increases when the owner invests more into the business (fresh capital) or when the business earns a profit (surplus). Introducing fresh capital directly increases the capital account. Paying a liability or buying an asset on credit does not affect owner's equity. Withdrawals decrease it.

May/June 2017

74. Which of the following will result in a decrease in a liability?
(A) Purchase of goods on credit.
(B) Taking a new bank loan.
(C) Owner investing more cash into the business.
(D) Payment to a creditor.

Ans :

(D) Payment to a creditor.
A liability represents an amount owed. To decrease a liability, the business must settle the obligation. Paying a creditor reduces the amount owed to that supplier, thus decreasing the 'Creditors' liability account. It also reduces the 'Cash' asset account by the same amount, keeping the balance sheet in equilibrium.

NODIA

Oct/Nov 2013

75. A transaction that increases one asset and decreases another asset by the same amount will:
(A) Have no effect on total assets.
(B) Increase total assets.
(C) Decrease total assets.
(D) Increase total liabilities.

Ans :

(A) Have no effect on total assets.
This type of transaction represents a change in the composition of assets. For example, buying machinery for cash decreases the cash asset but increases the machinery asset by an identical amount. The total value of all assets combined remains unchanged, and the liability/capital side is also unaffected.

May/June 2010

76. Identify the correct statement.
(A) Net Worth is the claim of outsiders against the assets of the business.
(B) If assets increase and liabilities do not, the capital will increase.
(C) All transactions of the business are recorded from the point of view of its owners.
(D) Assets are always equal to Capital.

(C) I and II only
(D) III only

Ans :

(C) I and II only
The relationship is Capital = Assets - Liabilities. Therefore, a reduction in capital can occur if assets decrease while liabilities remain constant, or if liabilities increase while assets remain constant. Both scenarios would lead to a smaller result for the owner's claim or capital. An increase in assets would increase capital.

Oct/Nov 2011

67. **Assertion (A) :** When a business pays for an expense like salary, its net worth decreases.
Reason (R) : The payment reduces an asset (cash) without creating another asset, and this reduction in value is absorbed by the owner's equity.
(A) Both A and R are true, and R is the correct explanation of A.
(B) Both A and R are true, but R is not the correct explanation of A.
(C) A is true, but R is false.
(D) A is false, but R is true.

Ans :

(A) Both A and R are true, and R is the correct explanation of A.
Paying an expense reduces cash, an asset. As the benefit is already consumed, no new asset is created. This net reduction in the asset side must be balanced by a reduction on the liabilities and capital side. Since no liability is reduced, the owner's equity (net worth) must decrease, as correctly explained in the reason.

May/June 2016

68. The text explains Transaction 5: "The business sells goods on credit for ₹5,000; the cost of the goods sold is ₹3,000." Which of the following is NOT an effect of this transaction?
(A) Cash increases by ₹5,000.
(B) A new asset, debtor, is created for ₹5,000.
(C) The stock of goods is reduced by ₹3,000.
(D) The owner's net worth increases by ₹2,000.

Ans :

(A) Cash increases by ₹5,000.
The transaction is a sale "on credit," which means payment is not received at the time of sale. Therefore, the cash balance is not affected at all. Instead, an asset called 'Debtor' is created to represent the amount receivable from the customer. All other listed effects are correct consequences of this transaction.

Oct/Nov 2008

69. What is the correct interpretation of the term 'Debtor' as used in the chapter?
(A) A person or entity from whom the business has borrowed money.
(B) A supplier to whom the business owes money for credit purchases.
(C) A customer who owes the business money for goods or services sold on credit.
(D) The owner of the business.

Ans :

(C) A customer who owes the business money for goods or services sold on credit.
A debtor is an asset for the business because it represents a legal claim to receive cash in the future. This situation arises when the business sells goods or provides services to a customer on credit, as illustrated in Transaction 5 where a debtor of ₹5,000 was created.

May/June 2022

70. What is the correct interpretation of the term 'Creditor' as used in the chapter?
(A) A person or entity to whom the business owes money.
(B) A customer who has paid in advance for goods.
(C) A customer who buys goods on credit.
(D) An employee to whom salary is payable.

Ans :

(A) A person or entity to whom the business owes money.
A creditor represents a liability for the business because it is an obligation to pay cash in the future. This situation arises when the business purchases goods, services, or assets on credit, as shown in Transaction 4, where a creditor of ₹5,000 was created after a credit purchase of goods.

Oct/Nov 2017

71. Consider the following statements about the balance sheet.
Statement I : The left-hand side shows the sources from which funds have been obtained.
Statement II : The right-hand side shows how

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(B) ₹22,000
(C) ₹26,000
(D) ₹21,000

Ans :

(D) ₹21,000
Net worth is the sum of Capital and Reserves & Surplus. In the final balance sheet (Balance Sheet 6), R's Capital is ₹20,000 and the Reserves & Surplus account stands at ₹1,000. Therefore, the total net worth of the owner at this point is ₹ 20,000 + ₹ 1,000 = ₹ 21,000.

May/June 2020

82. Which statement correctly analyses the change from Balance Sheet 3 to Balance Sheet 4?
(A) An asset was exchanged for another asset of equal value.
(B) An asset and a liability both increased by the same amount.
(C) An asset and owner's equity both increased by the same amount.
(D) An asset and a liability both decreased by the same amount.

Ans :

(B) An asset and a liability both increased by the same amount.
The transition from Balance Sheet 3 to 4 reflects the purchase of goods worth ₹5,000 on credit. This increased the asset 'Goods' from ₹2,000 to ₹7,000 (an increase of ₹5,000) and created a new liability 'Creditor' of ₹5,000. Both assets and liabilities increased, raising the balance sheet total to ₹25,000.

Oct/Nov 2022

83. Which statement correctly analyses the change from Balance Sheet 5 to Balance Sheet 6?
(A) An asset increased and a liability increased.
(B) An asset decreased and a liability decreased.
(C) An asset decreased and owner's equity decreased.
(D) One asset increased and another asset decreased.

Ans :

(C) An asset decreased and owner's equity decreased.
The change from Balance Sheet 5 to 6 is due to the payment of ₹1,000 in expenses. This transaction reduced the asset 'Cash' from ₹17,000 to ₹16,000. It also reduced the owner's equity, specifically the 'Reserves & Surplus' account, from ₹2,000 to ₹1,000.

May/June 2015

84. Mr. R's business is at the stage of Balance Sheet 6. The single debtor of ₹5,000 declares bankruptcy and is unable to pay anything. How would this event be recorded?
(A) Decrease Debtor by ₹5,000; Decrease Creditor by ₹5,000.
(B) Decrease Debtor by ₹5,000; Decrease R's Capital by ₹5,000.
(C) No entry is needed as no cash was exchanged.
(D) Decrease Debtor by ₹5,000; Decrease Reserves & Surplus by ₹5,000.

Ans :

(D) Decrease Debtor by ₹5,000; Decrease Reserves & Surplus by ₹5,000.
The inability to collect from a debtor means the asset 'Debtor' is now worthless and must be written off (decreased by ₹5,000). This loss must be borne by the business, which means it reduces the owner's equity. The loss is debited against the 'Reserves & Surplus' account, reducing it.

Oct/Nov 2015

85. A firm's balance sheet shows Assets of ₹5,00,000, Outside Liabilities of ₹2,00,000, and Capital of ₹3,00,000. If the firm purchases new equipment for ₹50,000 by taking a new loan, what will be the new balance sheet totals?
(A) Assets ₹5,50,000; Liabilities & Capital ₹5,50,000
(B) Assets ₹5,00,000; Liabilities & Capital ₹5,00,000
(C) Assets ₹5,50,000; Liabilities & Capital ₹5,00,000
(D) Assets ₹4,50,000; Liabilities & Capital ₹4,50,000

Ans :

(A) Assets ₹5,50,000; Liabilities & Capital ₹5,50,000
Purchasing equipment increases assets by ₹50,000 (from ₹5,00,000 to ₹5,50,000). Taking a loan to finance it increases outside liabilities by ₹50,000 (from ₹2,00,000 to ₹2,50,000). Capital remains ₹3,00,000. The new total liabilities and capital will be ₹ 2,50,000 + ₹ 3,00,000 = ₹ 5,50,000, matching the new total assets.

NODIA

May/June 2007

86. Which of the following is NOT an asset?
(A) Bills Receivable
(B) Bank Overdraft
(C) Stock in trade
(D) Machinery

Ans :

(B) Bank Overdraft
A bank overdraft occurs when a business withdraws more money from its bank account than is available, resulting in a negative balance. This amount is owed to the bank and is therefore a short-term liability, not an asset. All other options represent resources owned by the business.

Oct/Nov 2019

87. What does 'Reserves and Surplus' represent on the liability side of a balance sheet?
(A) Cash set aside for future emergencies.
(B) Money owed to suppliers for goods.
(C) The initial amount invested by the owner.
(D) The accumulated profits of the business that belong to the owner.

Ans :

(D) The accumulated profits of the business that belong to the owner.
'Reserves and Surplus' is the portion of the owner's equity that has been generated through profitable operations and retained within the business. It is distinct from the initial capital invested. It represents the increase in the owner's claim on assets resulting from the business's earnings over time.

May/June 2024

88. In the context of the balance sheet equation, 'Revenue' would lead to:
(A) An increase in assets and an increase in capital (surplus).
(B) A decrease in assets and a decrease in capital.
(C) An increase in liabilities and a decrease in capital.
(D) A decrease in assets and an increase in liabilities.

Ans :

(A) An increase in assets and an increase in capital (surplus).
Revenue is the income generated from business activities. Earning revenue typically increases an asset (like cash or debtors) and simultaneously increases the owner's equity (as profit or surplus). This is demonstrated in Transaction 5, where revenue from a sale increased both assets (net) and surplus.

Oct/Nov 2010

89. In the context of the balance sheet equation, an 'Expense' would lead to:
(A) An increase in assets and an increase in capital.
(B) An increase in assets and an increase in liabilities.
(C) A decrease in assets (or increase in liabilities) and a decrease in capital.
(D) No change in the balance sheet total.

Ans :

(C) A decrease in assets (or increase in liabilities) and a decrease in capital.
An expense is a cost incurred to generate revenue. It reduces the owner's equity (capital/surplus). This is balanced by either a decrease in an asset (like cash, as in Transaction 6) or an increase in a liability (if the expense is incurred on credit, e.g., outstanding salaries).

May/June 2013

90. Match the item to its correct classification.

	List I (Item)		**List II (Classification)**
P.	Bank Overdraft	1.	Owner's Equity
Q.	Debtor	2.	Asset
R.	R's Capital	3.	Outside Liability
S.	Goods	4.	Asset

(A) P-3, Q-2, R-1, S-4
(B) P-1, Q-2, R-3, S-4
(C) P-3, Q-4, R-1, S-2
(D) P-2, Q-3, R-1, S-4

Ans :

(A) P-3, Q-2, R-1, S-4
Bank Overdraft is an amount owed to the bank, making it an Outside Liability (3). Debtor is an amount receivable from a customer, an Asset (2). R's Capital is the owner's investment, which is Owner's Equity (1). Goods (stock) are resources held for sale, making them an Asset (4).

Oct/Nov 2021

91. Which of the following statements is INCORRECT?
(A) An asset is created by taking a liability of an

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equal amount.
(B) The sum of capital and reserves is called net worth.
(C) The business and its owners are considered two separate entities.
(D) Net worth is the claim of the creditors against the assets of the business.

Ans :

(D) Net worth is the claim of the creditors against the assets of the business.
This statement is incorrect. Net worth (Capital + Reserves) represents the claim of the owners against the assets of the business. The claim of the creditors (outsiders) against the assets is referred to as outside liabilities. All other statements are correct principles mentioned in the text.

May/June 2009

92. The initial transaction of Mr. R commencing business with ₹20,000 cash can be described as:
(A) An increase in assets and an increase in outside liabilities.
(B) An increase in assets and an increase in owner's equity.
(C) An exchange of one asset for another.
(D) A decrease in assets and a decrease in owner's equity.

Ans :

(B) An increase in assets and an increase in owner's equity.
When the owner invests cash, the business's asset (Cash) increases. Simultaneously, the owner's claim on the business (Capital, which is a component of owner's equity) increases by the same amount. This establishes the initial financial position and keeps the accounting equation in balance.

Oct/Nov 2006

93. Based on the data in 'Balance Sheet 3', calculate the value of Capital using the formula Capital = Assets - Outside Liabilities.

Liabilities	₹	Assets	₹
R's Capital	20,000	Cash	17,000
		Machinery	1,000
		Goods	2,000
Total	20,000	Total	20,000

(A) ₹17,000
(B) ₹3,000
(C) ₹20,000
(D) ₹0

Ans :

(C) ₹20,000
In 'Balance Sheet 3', the total assets are ₹17,000 (Cash) + ₹1,000 (Machinery) + ₹2,000 (Goods) = ₹20,000. There are no outside liabilities (Creditors, Loans etc.) at this stage, so their value is ₹0. Therefore, Capital = ₹ 20,000 (Assets) - ₹ 0 (Liabilities) = ₹ 20,000, which matches the figure shown.

May/June 2018

94. "A reduction in the amount of assets or an increase in the amount of liabilities will mean a reduction in the amount of capital." Which of the following transactions from the chapter exemplifies this principle?
(A) Purchase of machinery for cash.
(B) Purchase of goods on credit.
(C) Sale of goods on credit for a profit.
(D) Payment of rent and salaries.

Ans :

(D) Payment of rent and salaries.
The payment of rent and salaries (Transaction 6) caused a reduction in the asset 'Cash' by ₹1,00,0. Since this did not create another asset or reduce a liability, it resulted in a corresponding reduction of ₹1,00,0 in the owner's capital (specifically, the 'Reserves & Surplus' account).

Oct/Nov 2025

95. Suppose in Transaction 5, the goods costing ₹3,000 were sold for cash at ₹5,000 instead of on credit. What would be the balances of Cash and Surplus in the resulting balance sheet (starting from Balance Sheet 4)?
(A) Cash: ₹22,000; Surplus: ₹2,000
(B) Cash: ₹17,000; Surplus: ₹2,000
(C) Cash: ₹20,000; Surplus: ₹0
(D) Cash: ₹22,000; Surplus: ₹5,000

Ans :

(A) Cash: ₹22,000; Surplus: ₹2,000
Starting from Balance Sheet 4, the cash balance is ₹17,000. A cash sale of ₹5,000 would increase it to ₹ 17,000 + ₹ 5,000 = ₹ 22,000. The profit (surplus) is the selling price minus the cost (₹ 5,000 - ₹ 3,000 = ₹ 2,000), which increases owner's equity. No debtor account would be created.

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Ans :

(B) If assets increase and liabilities do not, the capital will increase.
Based on the equation Capital = Assets - Liabilities, if the 'Assets' value increases while 'Liabilities' remains constant, the resulting 'Capital' value must increase. This often occurs when a business earns revenue. The other statements are incorrect; net worth is the owner's claim, and transactions are recorded from the business's viewpoint.

Oct/Nov 2009

77. The balance sheet equation can also be expressed as "Outside Liabilities = Assets - Capital". If Assets are ₹90,000 and Capital is ₹65,000, what are the Outside Liabilities?
(A) ₹1,55,000
(B) ₹65,000
(C) ₹25,000
(D) ₹90,000

Ans :

(C) ₹25,000
Using the provided formula, Outside Liabilities = Assets - Capital. By substituting the given values, we calculate: Outside Liabilities = ₹ 90,000 - ₹ 65,000 = ₹ 25,000. This amount represents the total claims that external parties, such as suppliers and lenders, have on the business's assets.

May/June 2023

78. In Transaction 2, the business purchased machinery for ₹1,000. What would have been the effect if the machinery was purchased on credit instead of cash?
(A) Assets would increase by ₹1,000 and Liabilities would increase by ₹1,000.
(B) Assets would increase by ₹1,000 and Capital would increase by ₹1,000.
(C) Total assets would remain unchanged.
(D) Assets would decrease by ₹1,000 and Liabilities would decrease by ₹1,000.

Ans :

(A) Assets would increase by ₹1,000 and Liabilities would increase by ₹1,000.
If machinery is purchased on credit, the business acquires a new asset ('Machinery'), increasing total assets by ₹1,000. Since no cash is paid, a liability to the supplier ('Creditor' or 'Accounts Payable') is created, increasing total liabilities by ₹1,000. This would increase the balance sheet total to ₹21,000.

Oct/Nov 2024

79. Consider the following excerpt: "The business pays ₹500 for rent and ₹500 for salaries. The cash will now be reduced by ₹1,000. There is no asset to show for this. These expenses will be borne by the owner and to that extent the surplus will get reduced." What is the dual effect described here?
(A) Decrease in Asset (Cash) and Decrease in Liability (Creditor).
(B) Decrease in Asset (Cash) and Increase in Asset (Expenses).
(C) Decrease in Asset (Cash) and Decrease in Owner's Equity (Surplus).
(D) Decrease in Liability (Creditor) and Decrease in Owner's Equity (Surplus).

Ans :

(C) Decrease in Asset (Cash) and Decrease in Owner's Equity (Surplus).
The excerpt explicitly states that cash is reduced, which is a decrease in an asset. It also states that "the surplus will get reduced," which signifies a decrease in the owner's equity. This correctly identifies the two sides of the transaction required to keep the accounting equation in balance.

May/June 2014

80. Which of the following is the most accurate description of 'Capital' in the context of the balance sheet equation?
(A) The claim of the owners against the assets of the business.
(B) Cash available in the business.
(C) The total value of all business assets.
(D) The total amount owed to outside creditors.

Ans :

(A) The claim of the owners against the assets of the business.
Capital, along with reserves and surplus, represents the net worth or owner's equity. Due to the separate entity concept, it is viewed as the business's liability to its owners, or more accurately, the owners' residual claim on the assets after all outside liabilities have been settled.

Oct/Nov 2016

81. After all six transactions are completed, what is the final value of R's net worth?
(A) ₹20,000

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the repayment settles an obligation, which reduces the total outside liabilities. Both sides of the accounting equation decrease by the same amount, maintaining the balance but reducing the overall size of the balance sheet.

May/June 2019

102. Which of the following is a correct representation of Net Worth?
(A) Total Assets + Outside Liabilities
(B) Total Assets - Outside Liabilities
(C) Paid up Capital only
(D) Claims of creditors

Ans :

(B) Total Assets - Outside Liabilities
The fundamental equation is Assets = Outside Liabilities + Capital (or Net Worth). By rearranging this equation to solve for Net Worth, we get Net Worth = Assets - Outside Liabilities. This represents the residual interest of the owners in the assets of the entity after deducting all its liabilities.

Oct/Nov 2012

103. A transaction that increases an asset and increases a liability is:
(A) Sale of goods for cash.
(B) Payment of salary expense.
(C) Purchase of machinery on credit.
(D) Owner withdrawing cash for personal use.

Ans :

(C) Purchase of machinery on credit.
When machinery is purchased on credit, the business acquires an asset (machinery), causing total assets to increase. Since payment is deferred, a liability to the supplier (creditor) is created, causing total liabilities to increase by the same amount. This keeps the accounting equation in balance while expanding the balance sheet.

May/June 2012

104. The text provides a diagram illustrating the Balance Sheet Equation.
Assets side: Cash, Bank, Bills Receivable, Debtors, Stock in trade, Furniture, Machinery, Building.
Capital + Liabilities side: Capital + reserves and surplus, Creditors, Bills payable, Outstanding expenses, Bank Overdraft.
Which of the following is an INCORRECT classification according to this diagram?
(A) Bills payable as a Liability.
(B) Bills Receivable as an Asset.
(C) Bank Overdraft as a Liability.
(D) Outstanding expenses as an Asset.

Ans :

(D) Outstanding expenses as an Asset.
The diagram clearly places 'Outstanding expenses' on the 'Capital + Liabilities' side. Outstanding expenses represent costs incurred but not yet paid, creating an obligation for the business. Therefore, they are a liability, not an asset. All other classifications shown in the options are correct according to the diagram.

Oct/Nov 2007

105. Starting from the position of Balance Sheet 6, the business sells its entire machinery for ₹1,200 cash. What is the impact of this transaction?
(A) Cash increases by ₹1,200, Machinery decreases by ₹1,000, Surplus increases by ₹200.
(B) Cash increases by ₹1,200, Machinery decreases by ₹1,200.
(C) Cash increases by ₹200, Surplus increases by ₹200.
(D) Cash increases by ₹1,200, Capital increases by ₹1,200.

Ans :

(A) Cash increases by ₹1,200, Machinery decreases by ₹1,000, Surplus increases by ₹200.
The asset 'Machinery' has a book value of ₹1,000. Selling it removes this asset from the books. The business receives ₹1,200 cash, increasing the cash asset. The difference between the sale price (₹1,200) and the book value (₹1,000) is a profit of ₹200, which increases the owner's equity through the 'Surplus' account.

May/June 2025

106. A firm has Assets of ₹10,00,000 and Outside Liabilities of ₹4,00,000. The owner introduces an additional ₹1,00,000 cash as capital. What is the new value of the owner's capital?
(A) ₹6,00,000
(B) ₹7,00,000
(C) ₹5,00,000
(D) ₹11,00,000

Ans :

(B) ₹7,00,000
Initially, the owner's capital (net worth) is Assets - Liabilities = ₹ 10,00,000 - ₹ 4,00,000 = ₹ 6,00,000.

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May/June 2005

96. Which of the following represents the correct sequence of the balance sheet total for Mr. R's business after each of the first four transactions?
(A) ₹ 20,000 → ₹ 21,000 → ₹ 23,000 → ₹ 25,000
(B) ₹ 20,000 → ₹ 20,000 → ₹ 20,000 → ₹ 25,000
(C) ₹ 20,000 → ₹ 19,000 → ₹ 17,000 → ₹ 22,000
(D) ₹ 20,000 → ₹ 20,000 → ₹ 18,000 → ₹ 25,000

Ans :

(B) ₹ 20,000 → ₹ 20,000 → ₹ 20,000 → ₹ 25,000
1. Start with capital: Total is ₹20,000. 2. Buy machinery for cash: Total remains ₹20,000. 3. Buy goods for cash: Total remains ₹20,000. 4. Buy goods on credit: Total increases to ₹25,000. This sequence accurately reflects the impact of each transaction on the total size of the balance sheet.

Oct/Nov 2018

97. If a business has total claims of ₹8,00,000 and the claims of owners are ₹5,50,000, what is the value of the claims of creditors?
(A) ₹13,50,000
(B) ₹5,50,000
(C) Cannot be determined
(D) ₹2,50,000

Ans :

(D) ₹2,50,000
The total claims against a business are equal to the sum of the claims of owners and the claims of creditors. Therefore, Claims of Creditors = Total Claims - Claims of Owners. Substituting the values: ₹ 8,00,000 - ₹ 5,50,000 = ₹ 2,50,000. This represents the outside liabilities of the business.

May/June 2021

98. Consider the following statements:
Statement 1: Buying furniture for cash changes the total of the Balance Sheet.
Statement 2: Buying furniture on credit changes the total of the Balance Sheet.
(A) Only Statement 2 is correct.
(B) Only Statement 1 is correct.
(C) Both statements are correct.
(D) Neither statement is correct.

Ans :

(A) Only Statement 2 is correct.
Buying furniture for cash is an exchange of one asset (cash) for another (furniture), leaving the total assets unchanged. Buying furniture on credit increases an asset (furniture) and a liability (creditor), thus increasing the total of the balance sheet. Therefore, only the second statement is correct.

Oct/Nov 2014

99. Which of the following transactions will decrease total assets?
(A) Purchase of goods for cash.
(B) Cash received from a debtor.
(C) Payment of a creditor.
(D) Sale of goods on credit for a profit.

Ans :

(C) Payment of a creditor.
Paying a creditor involves a cash outflow, which decreases the asset 'Cash'. This is balanced by a decrease in the liability 'Creditors'. Consequently, the total assets of the business decrease. The other options either keep total assets the same or increase them.

May/June 2011

100. The equation 'Assets = Liabilities' as stated in the 'Let Us Sum Up' section implies that:
(A) The term 'Liabilities' here includes both outside liabilities and owner's capital.
(B) The business has no owner's capital.
(C) The business is bankrupt.
(D) The business has not made any profit or loss.

Ans :

(A) The term 'Liabilities' here includes both outside liabilities and owner's capital.
The summary states "Assets = Liabilities" will always be true and clarifies that "The liabilities consist of liabilities towards owners (Capital + Reserves and Surplus = Net worth) and towards outsiders." This means the term 'Liabilities' is used in its broadest sense to encompass all claims against the assets.

Oct/Nov 2005

101. What is the effect of repayment of a loan on the balance sheet?
(A) It increases both assets and liabilities.
(B) It increases assets and decreases liabilities.
(C) It has no effect on total assets and liabilities.
(D) It decreases both assets and liabilities.

Ans :

(D) It decreases both assets and liabilities.
Repaying a loan requires an outflow of cash, which reduces the total assets. Simultaneously,

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(A) Going Concern Concept
(B) The Business Entity Concept
(C) Accrual Concept
(D) Materiality Concept

Ans :

(B) The Business Entity Concept
The Business Entity Concept treats the business as an artificial person, separate and distinct from its owners. Because of this separation, any funds invested by the owners are considered an amount that the business 'owes' back to them. Hence, net worth is classified as a liability of the business.

Oct/Nov 2017

113. If a business purchases a new building for ₹5,00,000, paying ₹2,00,000 in cash and taking a loan for the balance ₹3,00,000, what is the net effect on the accounting equation?
(A) Total Assets increase by ₹5,00,000 and Liabilities increase by ₹5,00,000.
(B) Total Assets increase by ₹2,00,000 and Liabilities increase by ₹2,00,000.
(C) Total Assets increase by ₹3,00,000 and Liabilities increase by ₹3,00,000.
(D) Total Assets and Liabilities remain unchanged.

Ans :

(C) Total Assets increase by ₹3,00,000 and Liabilities increase by ₹3,00,000.
Assets change by +₹ 5,00,000 (Building) and -₹ 2,00,000 (Cash), for a net increase of ₹3,00,000. Liabilities increase by ₹3,00,000 due to the new loan. Therefore, both the asset side and the liability side increase by ₹3,00,000, keeping the equation balanced.

May/June 2008

114. In Balance Sheet 5, the total assets are ₹27,000. What is the value of owner's equity at this stage?
(A) ₹27,000
(B) ₹20,000
(C) ₹5,000
(D) ₹22,000

Ans :

(D) ₹22,000
In Balance Sheet 5, the owner's equity (or net worth) is the sum of 'R's Capital' and 'Reserves & Surplus'. The values are ₹20,000 and ₹2,000 respectively. Therefore, the total owner's equity is ₹ 20,000 + ₹ 2,000 = ₹ 22,000. The remaining ₹5,000 on the liability side is an outside liability (Creditor).

Oct/Nov 2023

115. Mr. R's business, in the state of Balance Sheet 6, receives the full payment of ₹5,000 from its debtor. Immediately after, it repays its creditor of ₹5,000. What is the net effect of these two transactions on the Cash balance?
(A) Cash balance remains unchanged.
(B) Cash increases by ₹5,000.
(C) Cash decreases by ₹5,000.
(D) Cash balance becomes zero.

Ans :

(A) Cash balance remains unchanged.
The first transaction (receiving from debtor) increases cash by ₹5,000. The second transaction (paying the creditor) decreases cash by ₹5,000. The net effect on the cash balance is an increase of ₹5,000 followed by a decrease of ₹5,000, resulting in a zero net change to the cash account.

May/June 2017

116. "If assets increase and liabilities do not, the capital will increase". Which transaction in the chapter is a direct example of this?
(A) None, as this scenario is not possible.
(B) The profit element of Transaction 5 (sale of goods on credit).
(C) Transaction 4 (purchase of goods on credit).
(D) Transaction 2 (purchase of machinery for cash).

Ans :

(B) The profit element of Transaction 5 (sale of goods on credit).
In Transaction 5, total assets had a net increase of ₹2,000 (Debtor of ₹5,000 created, Goods of ₹3,000 removed). This net increase in assets, with no change in outside liabilities, was balanced by a ₹2,000 increase in capital (Surplus), perfectly illustrating the principle.

Oct/Nov 2013

117. **Assertion (A) :** The purchase of machinery for cash does not change the total liabilities of a firm.
Reason (R) : This transaction only involves the conversion of one asset (cash) into another asset (machinery).
(A) Both A and R are true, and R is the correct explanation of A.
(B) Both A and R are true, but R is not the correct

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₹1,000
(B) Goods: ₹3,000; Debtors: ₹5,000; Surplus: ₹1,500
(C) Goods: ₹5,000; Debtors: ₹6,500; Surplus: ₹1,000
(D) Goods: ₹3,000; Debtors: ₹6,500; Surplus: ₹1,500

Ans :

(D) Goods: ₹3,000; Debtors: ₹6,500; Surplus: ₹1,500
Starting from Balance Sheet 6: Goods balance is ₹4,000, it will decrease by the cost of ₹1,000 to ₹3,000. Debtors balance is ₹5,000, it will increase by the sale value of ₹1,500 to ₹6,500. Surplus balance is ₹1,000, it will increase by the profit (₹ 1,500 - ₹ 1,000 = ₹ 500) to ₹1,500.

May/June 2007

128. The relationship `Capital = Assets - Outside Liabilities` shows that capital is a:
(A) Residual claim on assets.
(B) Fixed claim on assets.
(C) Primary claim on assets.
(D) Non-existent claim on assets.

Ans :

(A) Residual claim on assets.
The formula implies that the owner's capital is what is left over after the claims of all outsiders (liabilities) have been subtracted from the total assets. This defines the owner's claim as a residual one; they are entitled to the net assets of the business after all other obligations are met.

Oct/Nov 2019

129. Identify the transaction that affects only one side of the accounting equation (Assets = Liabilities + Capital).
(A) Purchase of goods on credit.
(B) Payment of salaries in cash.
(C) Purchase of machinery for cash.
(D) Sale of goods on credit for a profit.

Ans :

(C) Purchase of machinery for cash.
Purchasing machinery for cash involves decreasing one asset (Cash) and increasing another asset (Machinery) by the same amount. The entire transaction is contained within the 'Assets' side of the equation. All other options affect both sides of the equation (Assets and Liabilities, or Assets and Capital).

May/June 2024

130. A company's assets increased by ₹1,00,000 and its liabilities increased by ₹40,000 during a year. What was the change in the owner's equity for the year?
(A) Increased by ₹60,000
(B) Decreased by ₹60,000
(C) Increased by ₹1,40,000
(D) Decreased by ₹1,40,000

Ans :

(A) Increased by ₹60,000
The change in assets must equal the change in liabilities plus the change in owner's equity. So, +₹ 1,00,000 = +₹ 40,000 + Change in Equity. To find the change in equity, we calculate ₹ 1,00,000 - ₹ 40,000 = ₹ 60,000. This increase in equity could be due to profits or additional capital investment.

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May/June 2014

122. At the stage of Balance Sheet 2, Mr. R realizes the machinery purchased for ₹1,000 is faulty and returns it, receiving a full cash refund. What is the state of the balance sheet after this reversal?
(A) Assets (Cash ₹19,000, Machinery ₹1,000), Capital ₹20,000.
(B) Assets (Cash ₹20,000), Capital ₹20,000.
(C) Assets (Cash ₹20,000), Capital ₹19,000, Surplus ₹1,000.
(D) Assets (Cash ₹19,000), Capital ₹19,000.

Ans :

(B) Assets (Cash ₹20,000), Capital ₹20,000.
This transaction reverses the original purchase. The asset 'Machinery' decreases by ₹1,000 (from ₹1,000 to zero), and the asset 'Cash' increases by ₹1,000 (from ₹19,000 to ₹20,000). The business returns to its initial state as shown in Balance Sheet 1, with only Cash as an asset.

Oct/Nov 2016

123. Which of the following situations will NOT change the total value of assets?
(A) Sale of goods for cash at a price higher than cost.
(B) Purchase of goods on credit.
(C) Collection of cash from debtors.
(D) Payment of an outstanding expense.

Ans :

(C) Collection of cash from debtors.
Collecting cash from debtors is a transaction where one current asset (Debtors) is converted into another current asset (Cash). The total value of assets remains the same, although their composition changes. All other options involve a change in either liabilities or owner's equity, which affects the total assets.

May/June 2020

124. The final balance sheet (Balance Sheet 6) shows total assets of ₹26,000. This value represents:
(A) The profits earned by the business.
(B) The total amount owed to outsiders.
(C) The net worth of the business.
(D) The total investment of funds into various business resources.

Ans :

(D) The total investment of funds into various business resources.
The asset side of the balance sheet details the application or use of funds. The total of ₹26,000 represents the sum of all resources (Cash, Machinery, Goods, Debtor) that the business has invested in and controls at that point in time, using funds from both owners and outsiders.

Oct/Nov 2022

125. If a firm's Balance Sheet shows Total Assets of ₹15,00,000 and Net Worth of ₹9,00,000, what percentage of the assets are financed by outside liabilities?
(A) 40%
(B) 60%
(C) 100%
(D) 66.67 %

Ans :

(A) 40%
First, find the value of outside liabilities: Assets - Net Worth = ₹ 15,00,000 - ₹ 9,00,000 = ₹ 6,00,000. To find the percentage financed by these liabilities, divide the liabilities by total assets: (₹ 6,00,000 / ₹ 15,00,000) times 100 = 40%. This means 40% of the firm's resources are funded by creditors.

May/June 2015

126. In the context of the explanation for Transaction 5, what does the term 'surplus' signify?
"The net increase in the asset ₹2,000 (₹5,000 less ₹3,000) is a surplus which belongs to the owner."
(A) Excess goods that were not sold.
(B) The profit earned from the sale transaction.
(C) The cash received from the customer.
(D) A new liability created from the sale.

Ans :

(B) The profit earned from the sale transaction.
The excerpt calculates the 'surplus' as the difference between the sale value (₹5,000) and the cost of the goods (₹3,000). This difference is the definition of gross profit on a sale. The text correctly identifies this surplus as belonging to the owner, thereby increasing their net worth.

Oct/Nov 2015

127. Mr. R's business is at the final stage (Balance Sheet 6). He is considering selling goods that cost ₹1,000 for ₹1,500 on credit. If this transaction occurs, what will be the new balances for Goods, Debtors, and Surplus?
(A) Goods: ₹4,000; Debtors: ₹5,000; Surplus:

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explanation of A.
(C) A is true, but R is false.
(D) A is false, but R is true.

Ans :

(A) Both A and R are true, and R is the correct explanation of A.
The assertion is true; total liabilities are unaffected. The reason correctly explains why: the transaction is confined entirely to the asset side of the balance sheet. Since there is no interaction with the liability or capital accounts, their totals remain unchanged. The reason provides a complete explanation for the assertion.

May/June 2010

118. Which of the following will always be true for a business entity?
I. Assets = Capital + Reserves and Surplus + Creditors
II. Assets = Net Worth + Outside Liabilities
III. Capital = Assets - Outside Liabilities
IV. Assets - Capital - Outside Liabilities = 0
(A) I and II only
(B) I, II and IV only
(C) II and III only
(D) All I, II, III and IV are correct.

Ans :

(B) I, II and IV only
Statement I is the expanded equation. Statement II is the condensed form, as Net Worth = Capital + Reserves. Statement IV is a simple rearrangement of the basic equation. Statement III (Capital = Assets - Outside Liabilities) is only true if there are no reserves or surplus, otherwise Capital + Reserves = Assets - Outside Liabilities.

Oct/Nov 2009

119. A transaction where an owner brings his personal car worth ₹2,00,000 into the business for official use will result in:
(A) Increase in Assets (Car) by ₹2,00,000; Increase in Liabilities (Loan) by ₹2,00,000.
(B) No change in the Balance Sheet as no cash was involved.
(C) Increase in Assets (Car) by ₹2,00,000; Increase in Capital by ₹2,00,000.
(D) Increase in Assets (Car) by ₹2,00,000; Decrease in Assets (Cash) by ₹2,00,000.

Ans :

(C) Increase in Assets (Car) by ₹2,00,000; Increase in Capital by ₹2,00,000.
When an owner contributes a non-cash asset to the business, it is treated as an additional capital investment. The business gains an asset (Car), and the owner's claim against the business (Capital) increases by the fair value of the asset contributed. This maintains the balance sheet equality.

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May/June 2023

120. The text states: "The total claims...against a business will always equal the total assets of the business." This principle is best demonstrated by which of the following?
(A) The total of Liabilities side always matches the total of Assets side in all 6 balance sheets.
(B) The owner's capital remains fixed at ₹20,000.
(C) The cash balance continuously decreases.
(D) The business makes a profit in one transaction.

Ans :

(A) The total of Liabilities side always matches the total of Assets side in all 6 balance sheets.
This principle is the very definition of the balance sheet equation. The fact that in every single balance sheet presented (from 1 to 6), the final total of the 'Liabilities' column is exactly equal to the final total of the 'Assets' column provides a consistent, practical demonstration of this rule.

Oct/Nov 2024

121. What is the fundamental reason that 'Capital' is treated as a liability in the balance sheet equation?
(A) Because the owner is expected to take the money back at any time.
(B) To ensure that the balance sheet total is as high as possible.
(C) It is a legal requirement by tax authorities.
(D) Due to the business entity concept, which treats the business as separate from its owner.

Ans :

(D) Due to the business entity concept, which treats the business as separate from its owner.
The business entity concept is the accounting principle that requires a separation between the business's affairs and the owner's personal affairs. From the business's perspective, the money invested by the owner is an amount it owes to the owner, hence it is classified as a liability or equity.

CHAPTER 13

Preparation of Final Accounts

Oct/Nov 2025

1. What is the ultimate objective of recording financial transactions in a business enterprise?

(A) To calculate the total cash flow during the accounting period.

(B) To prepare the balance sheet and the P&L account for stakeholders.

(C) To maintain a detailed record of all individual customer transactions.

(D) To ensure compliance with tax regulations only.

Ans :

(B) To prepare the balance sheet and the P&L account for stakeholders.

The primary goal of the accounting process is to prepare the final accounts, namely the balance sheet and the profit and loss (P&L) account. These statements provide stakeholders with a fair view of the operational results and the financial position of the enterprise at the end of the accounting period, typically a year.

May/June 2012

2. What do the final accounts of a business enterprise primarily show?

(A) The final results in terms of profit or loss and the financial position of assets and liabilities.

(B) The day-to-day operational efficiency of the management team.

(C) The projected future earnings and growth prospects of the business.

(D) The total number of transactions processed during the accounting period.

Ans :

(A) The final results in terms of profit or loss and the financial position of assets and liabilities.

Final accounts are prepared at the end of an accounting period to summarize the business's performance and position. They reveal the profit earned or loss sustained during the period through the P&L account and present a snapshot of the company's assets and liabilities at that specific date through the balance sheet.

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Oct/Nov 2014

3. In a manual bookkeeping system, what was the primary purpose of preparing a trial balance?

(A) To determine the final profit or loss of the business.

(B) To serve as the primary financial statement for external auditors.

(C) To find out whether any posting or mathematical errors were made.

(D) To calculate the value of closing stock at the end of the year.

Ans :

(C) To find out whether any posting or mathematical errors were made.

Historically, in manual accounting systems, the trial balance was a crucial tool used to check the arithmetical accuracy of the ledger. It helped accountants identify clerical errors related to posting transactions or mathematical mistakes in balancing accounts before proceeding to prepare the final financial statements. Its primary role was error detection.

May/June 2019

4. In the context of modern accounting software, what is the continuing importance of a trial balance?

(A) It is the only way to detect software bugs in the accounting system.

(B) It is a mandatory financial statement required by law for all businesses.

(C) It automatically calculates and posts all necessary adjustment entries.

(D) It allows accountants and auditors to view GL account balances before and after adjustments.

Ans :

(D) It allows accountants and auditors to view GL account balances before and after adjustments.

While accounting software has eliminated most clerical and mathematical errors, the trial balance remains important. It provides a clear summary of all general ledger account balances.

This is particularly useful for accountants and auditors who need to see the state of the accounts before and after proposed adjustments are made, facilitating analysis and verification.

Oct/Nov 2006

5. Which of the following statements about a trial balance is correct?
(A) It is considered a primary financial statement of a business enterprise.
(B) It is prepared after making all the adjustment entries.
(C) By itself, a trial balance, whether adjusted or unadjusted, is not a financial statement.
(D) It primarily lists the assets and liabilities of the business.

Ans :

(C) By itself, a trial balance, whether adjusted or unadjusted, is not a financial statement.
A trial balance is an internal document, a worksheet that lists all ledger account balances. Its purpose is to verify the equality of debits and credits and to act as a starting point for preparing financial statements. However, it is not a formal financial statement like the P&L account or the balance sheet.

May/June 2021

6. Why are adjustment entries necessary in accounting?
(A) To correct fraudulent transactions recorded during the year.
(B) To account for transactions that span more than one accounting period.
(C) To record cash transactions that were missed during the year.
(D) To transfer balances from the P&L account to the balance sheet.

Ans :

(B) To account for transactions that span more than one accounting period.
Adjustment entries are required to ensure that the financial statements reflect the revenues earned and expenses incurred during a specific accounting period, regardless of when the cash is exchanged. They address timing differences, such as accrued expenses or prepaid income, thereby ensuring adherence to the accrual basis of accounting and presenting a fair picture.

Oct/Nov 2010

7. If rent for March 2022 is paid in April 2022, what is the effect on the Profit and Loss account for the year ended March 31, 2022, if no adjustment entry is made?
(A) The profit will be understated.
(B) The profit will not be affected.
(C) The sales figure will be incorrect.
(D) The profit will be inflated.

Ans :

(D) The profit will be inflated.
If the rent expense for March 2022 is not accounted for within the financial year ending March 31, 2022, the total expenses for that period will be understated. An understatement of expenses leads to an overstatement or inflation of the calculated profit, which does not provide a fair and accurate view of the company's performance.

May/June 2005

8. When an adjustment entry for unpaid rent of ₹5,000 is made, the 'Rent Paid' account is debited. Which account is correspondingly credited?
(A) A liability account like 'Rent Payable'.
(B) An asset account like 'Prepaid Rent'.
(C) An income account like 'Rent Received'.
(D) The 'Cash' account.

Ans :

(A) A liability account like 'Rent Payable'.
The adjustment entry for an outstanding expense involves recognizing the expense and the corresponding liability. Debiting the 'Rent Paid' account recognizes the expense for the period. Crediting a liability account, such as 'Rent Payable', acknowledges the company's obligation to pay this amount in the future, which will be reflected on the balance sheet.

Oct/Nov 2022

9. According to Accounting Standard (AS-1) and Indian Accounting Standard (Ind AS-1), which fundamental accounting assumption necessitates the use of adjustment entries?
(A) Going Concern assumption
(B) Consistency assumption
(C) Accrual assumption
(D) Business Entity assumption

Ans :

(C) Accrual assumption

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Both AS-1 and Ind AS-1 identify accrual as a fundamental accounting assumption. This principle requires that revenues and expenses be recognized as they are earned or incurred, not necessarily when cash is received or paid. Adjustment entries are the mechanism used to align the accounting records with this accrual basis before preparing financial statements.

May/June 2018

10. Adjusting entries almost always involve a combination of which two types of accounts?
(A) A balance sheet account and a P&L account.
(B) Two different balance sheet accounts.
(C) Two different P&L accounts.
(D) A cash account and a non-cash account.

Ans :

(A) A balance sheet account and a P&L account.
The purpose of an adjusting entry is to correctly state both the period's income/expense and the year-end financial position. Therefore, these entries typically affect one income statement (P&L) account (like Rent Expense, Interest Income) and one balance sheet account (like Rent Payable, Interest Receivable), ensuring both statements are accurate under the accrual basis.

Oct/Nov 2016

11. What is the correct adjustment entry for a salary of ₹50,000 for March that has been incurred but will be paid in April?
(A) Debit 'Salary Payable' account and Credit 'Salary' account.
(B) Debit 'Cash' account and Credit 'Salary Payable' account.
(C) Debit 'Salary' account and Credit 'Cash' account.
(D) Debit 'Salary' account and Credit 'Salary Payable' account.

Ans :

(D) Debit 'Salary' account and Credit 'Salary Payable' account.
To account for an expense incurred but not yet paid (an outstanding expense), the expense must be recognized in the current period. This is done by debiting the relevant expense account (Salary account). Simultaneously, a liability is created to reflect the obligation to pay, which is achieved by crediting a liability account (Salary Payable account).

May/June 2014

12. If a company pays insurance for a full year in advance, how should the portion of the insurance that has not yet been incurred be treated at the end of the accounting period?
(A) It is treated as an expense for the current period.
(B) It is treated as an asset, and the recipient is considered a debtor.
(C) It is treated as a loss and written off from the P&L account.
(D) It is treated as a liability until the service is rendered.

Ans :

(B) It is treated as an asset, and the recipient is considered a debtor.
When an expense is paid in advance, the portion that pertains to a future accounting period is not an expense of the current period. It represents a future economic benefit and is therefore classified as a prepaid expense, which is an asset on the balance sheet. The entity that received the payment owes a service.

Oct/Nov 2007

13. How should interest accrued on a fixed deposit, which will be paid on maturity, be accounted for at the end of the financial year?
(A) Debit 'Interest Income' account and Credit 'Bank' account.
(B) Debit 'Fixed Deposit' account and Credit 'Interest Income' account.
(C) Debit 'Interest Receivable' account and Credit 'Interest Income' account.
(D) No entry is passed until the interest is actually received.

Ans :

(C) Debit 'Interest Receivable' account and Credit 'Interest Income' account.
Under the accrual basis of accounting, income that has been earned but not yet received must be recognized. The 'Interest Income' account is credited to recognize the income for the period. The 'Interest Receivable' account, which is an asset account, is debited to show the amount that the bank owes to the company.

May/June 2025

14. A company receives advance rent from a tenant in March for the month of April. What is the

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correct adjustment entry to be passed on March 31st?
(A) Debit 'Cash' account and Credit 'Advance Rent Received' account.
(B) Debit 'Advance Rent Received' account and Credit 'Rent Received' account.
(C) Debit 'Rent Receivable' account and Credit 'Rent Received' account.
(D) Debit 'Rent Received' account and Credit 'Advance Rent Received' account.

Ans :

(D) Debit 'Rent Received' account and Credit 'Advance Rent Received' account.
The rent received in advance is not income for the current period (ending in March). It is a liability, as the service (use of property) is owed for April. The initial entry would have credited 'Rent Received'. The adjustment entry reverses this by debiting 'Rent Received' and crediting 'Advance Rent Received' (a liability account).

Oct/Nov 2019

15. **Assertion (A) :** Adjusting entries are necessary to convert a company's accounting records to the accrual basis of accounting.
Reason (R) : The accrual basis requires that all cash transactions within a period must be recorded as income or expenses for that period.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(C) (A) is true but (R) is false.
Assertion (A) is true; adjusting entries are fundamental to implementing the accrual basis. However, Reason (R) is false because it misrepresents the accrual concept. Accrual accounting recognizes revenues when earned and expenses when incurred, irrespective of the timing of cash flows, which is the opposite of what the reason states.

May/June 2009

16. A company borrowed money from a bank on March 1, 2022, with the first interest payment due on June 1, 2022. For the financial year ending March 31, 2022, what adjustment is required?
(A) No entry is needed as no interest has been paid.
(B) An entry to debit Interest Expense and credit Interest Payable for one month's interest.
(C) An entry to debit Interest Expense and credit Cash for one month's interest.
(D) An entry to debit Loan account and credit Interest Payable for one month's interest.

Ans :

(B) An entry to debit Interest Expense and credit Interest Payable for one month's interest.
Although the cash payment will occur later, the company has incurred an interest expense for the month of March. To accurately report the company's profit and liabilities as of March 31, an adjusting entry must be made to recognize this expense (debit Interest Expense) and the corresponding liability (credit Interest Payable) for one month.

Oct/Nov 2011

17. Which of the following is NOT a typical adjustment entry relating to income and expenditure?
(A) Accounting for salary incurred but not paid.
(B) Accounting for the purchase of a fixed asset on credit.
(C) Accounting for insurance paid in advance.
(D) Accounting for rent received in advance.

Ans :

(B) Accounting for the purchase of a fixed asset on credit.
The purchase of a fixed asset on credit is a standard financial transaction recorded at the time it occurs by debiting the asset account and crediting a liability (creditor/vendor account). It is not an adjustment entry, which is typically made at the end of an accounting period to account for timing differences like accruals and prepayments.

May/June 2010

18. Which of the following statements is incorrect regarding adjustment entries?
(A) They are the result of a specific financial transaction occurring at year-end.
(B) They are made just prior to preparing the financial statements.
(C) They are needed to present a fair and correct picture of the business.
(D) They help in converting accounting records to the accrual basis.

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Ans :

(A) They are the result of a specific financial transaction occurring at year-end.
Adjustment entries are not the result of a new financial transaction. Instead, they are internal entries made to adjust accounts for revenues and expenses that have been earned or incurred in one period but for which cash will be exchanged in another. They are adjustments, not new transactions with external parties.

Oct/Nov 2024

19. If a business has incurred an expense but not yet paid for it, what is this type of expense called?
(A) Prepaid Expense
(B) Accrued Income
(C) Outstanding Expense
(D) Unearned Income

Ans :

(C) Outstanding Expense
An outstanding expense, also known as an accrued expense, is a cost that a business has incurred during an accounting period but has not yet paid for. Examples include salaries for the last month of the year paid in the next year or utility bills received but not yet paid. It is recorded as a current liability.

May/June 2017

20. When income has been received but is not yet earned, how is it classified in the balance sheet?
(A) As a current liability.
(B) As a non-current asset.
(C) As a current asset.
(D) As part of owner's equity.

Ans :

(A) As a current liability.
Income received but not yet earned is known as unearned or advance income. Since the business has received cash but has not yet provided the corresponding goods or services, it has an obligation to the customer. This obligation is recorded as a current liability on the balance sheet until the income is officially earned.

Oct/Nov 2005

21. What is the primary purpose of preparing financial statements like the P&L account and Balance Sheet from a trial balance?
(A) To verify the arithmetical accuracy of the ledger one last time.
(B) To create a list of all asset and liability accounts for internal audit.
(C) To close all the personal and real accounts in the general ledger.
(D) To find out the operational results and financial position of the business.

Ans :

(D) To find out the operational results and financial position of the business.
After ensuring arithmetical accuracy with a trial balance and making necessary adjustments, the primary goal is to prepare the final financial statements. The Profit & Loss account is prepared to determine the operational results (profit or loss), and the Balance Sheet is prepared to show the entity's financial position at the year's end.

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May/June 2020

22. Depreciation is described as a reduction in the value of fixed assets. Which of the following assets is generally considered an exception to this rule?
(A) Buildings
(B) Land
(C) Machinery
(D) Computer Systems

Ans :

(B) Land
Depreciation applies to most fixed assets due to factors like wear and tear, usage, or obsolescence. However, land is a notable exception. Its value generally does not decrease over time due to use; in fact, it often appreciates. Therefore, depreciation is not typically charged on land as an asset.

Oct/Nov 2015

23. How is depreciation classified as an expense?
(A) It is a cash expense paid to an external party.
(B) It is a contingent expense, recorded only if the company is profitable.
(C) It is an actual expense, though not a cash expense.
(D) It is a fictitious expense with no impact on actual profit.

Ans :

(C) It is an actual expense, though not a cash expense.
Depreciation is the systematic allocation of the cost of a tangible asset over its useful life.

Although no cash is paid out when depreciation is recorded, it represents the real economic cost of the asset being used up. Therefore, it is an actual, non-cash expense that must be deducted to arrive at the true profit.

May/June 2013

24. What is the standard accounting entry to record depreciation on a fixed asset?
(A) Debit the Fixed Asset account and Credit the Depreciation account.
(B) Debit the Cash account and Credit the Depreciation account.
(C) Debit the P&L Appropriation account and Credit the Fixed Asset account.
(D) Debit the Depreciation account and Credit the Fixed Asset account.

Ans :

(D) Debit the Depreciation account and Credit the Fixed Asset account.
To record depreciation, an expense must be recognized. This is done by debiting the Depreciation account, which is an expense account transferred to the P&L account. The value of the asset decreases, so the Fixed Asset account is credited, reducing its debit balance. This correctly reflects the consumption of the asset's economic value.

Oct/Nov 2021

25. What is the purpose of the 'Accumulated Depreciation' account?
(A) To act as a contra-asset account that accumulates total depreciation charged on an asset.
(B) To record the original purchase price and installation cost of all fixed assets.
(C) To act as a sinking fund by setting aside cash for the future replacement of an asset.
(D) To directly reduce the owner's capital account by the amount of depreciation expense.

Ans :

(A) To act as a contra-asset account that accumulates total depreciation charged on an asset.
Instead of directly crediting the fixed asset account, companies often credit a separate account called 'Accumulated Depreciation'. This is a contra-asset account, meaning its credit balance is netted against the debit balance of the related fixed asset on the balance sheet. This method preserves the original cost of the asset in the records.

May/June 2024

26. What is the term used for providing for the reduction in the value of intangible assets and long-term investments?
(A) Depletion
(B) Amortisation
(C) Obsolescence
(D) Impairment

Ans :

(B) Amortisation
While the term depreciation is used for tangible fixed assets like machinery and buildings, the systematic write-off of the cost of intangible assets (like patents, copyrights) and long-term investments over their useful life is generally referred to as amortisation. It is conceptually similar to depreciation but applies to non-physical assets.

Oct/Nov 2008

27. Which Indian Accounting Standard (Ind AS) provides guidelines regarding the depreciation of tangible fixed assets?
(A) Ind AS 38
(B) Ind AS 2
(C) Ind AS 1
(D) Ind AS 16

Ans :

(D) Ind AS 16
Indian Accounting Standard (Ind AS) 16 specifically deals with the accounting for Property, Plant, and Equipment, which are tangible fixed assets. This standard provides detailed guidelines on their recognition, measurement, and importantly, the methods and principles for calculating and recording their depreciation over their useful lives. Ind AS 38 covers intangible assets.

May/June 2006

28. Which accounting standards deal with the accounting of tangible and intangible fixed assets respectively?
(A) AS-10 and AS-26
(B) AS-26 and AS-10
(C) AS-1 and AS-2
(D) AS-16 and AS-38

Ans :

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(A) AS-10 and AS-26
Accounting Standard (AS) 10, "Property, Plant and Equipment," deals with the accounting for tangible fixed assets. Accounting Standard (AS) 26, "Intangible Assets," provides the guidelines for accounting for intangible assets. These standards cover aspects from recognition and measurement to depreciation and amortisation, respectively.

Oct/Nov 2017

29. When purchase or sales transactions are recorded in the ledger, which account is typically NOT affected by these entries throughout the year?
(A) The Purchase Account
(B) The Sales Account
(C) The Stock Account
(D) The Cash Account

Ans :

(C) The Stock Account
In a periodic inventory system, entries for purchases are debited to the 'Purchase Account' and sales are credited to the 'Sales Account'. These transactions do not directly impact the 'Stock Account' during the accounting period. The balance in the 'Stock Account' continues to reflect the opening stock value until an adjustment is made for closing stock.

May/June 2008

30. The formula for profit is given as: Profit = sales – (purchases + opening stock – closing stock + expenses) . Which item in this formula is NOT typically available from the ledger balances?
(A) Closing stock
(B) Sales
(C) Purchases
(D) Expenses

Ans :

(A) Closing stock
The values for sales, purchases, opening stock (which is the previous year's closing stock), and expenses are all available from the respective ledger account balances. However, the value of closing stock is not recorded during the year. It must be determined by a physical count and valuation at the end of the accounting period.

Oct/Nov 2013

31. What is the process of physically verifying and valuing the available stock at the close of the year called?
(A) Stock Auditing
(B) Asset Verification
(C) Stock Reconciliation
(D) Inventory Valuation

Ans :

(D) Inventory Valuation
Inventory valuation is the specific process of determining the monetary value of inventory at the end of an accounting period. This involves two steps: first, physically counting the items in stock, and second, assigning a value to them based on an accepted accounting principle, which is crucial for calculating profit and presenting the correct financial position.

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May/June 2015

32. What is the direct impact of an overvaluation of closing stock on the firm's reported profit?
(A) It results in understating the profit.
(B) It results in inflating the profit.
(C) It has no impact on the profit, only on the balance sheet.
(D) It decreases the gross profit but increases the net profit.

Ans :

(B) It results in inflating the profit.
In the profit calculation, closing stock is deducted from the cost of goods available for sale. If the closing stock value is overstated (inflated), the cost of goods sold will be understated. A lower cost of goods sold directly leads to a higher reported gross profit and, consequently, a higher net profit.

Oct/Nov 2012

33. According to accounting principles, what is the correct basis for the valuation of closing stock?
(A) The purchase cost only.
(B) The market value only.
(C) The lower of the purchase cost or market value.
(D) The higher of the purchase cost or market value.

Ans :

(C) The lower of the purchase cost or market value.

(D) Statement of Changes in Equity

Ind AS-1 replaces the traditional P&L Appropriation Account with a more comprehensive "Statement of Changes in Equity". This statement is more detailed, as it not only shows appropriations like dividends and reserve transfers but also incorporates transactions with owners in their capacity as owners, such as the issue of new shares.

Oct/Nov 2007

55. What is the fundamental difference between the money invested by promoters (capital) and money received as a loan from creditors?

(A) Business losses result in a reduction of capital but do not affect the amount to be repaid to creditors.

(B) Capital is a long-term liability, while loans from creditors are always required to be short-term liabilities.

(C) Loans from creditors carry a fixed rate of interest, whereas capital does not have a pre-determined rate of return.

(D) The amount of capital must be repaid in full upon request, whereas loan amounts are only repaid if the business is profitable.

Ans :

(A) Business losses result in a reduction of capital but do not affect the amount to be repaid to creditors.

Capital, or risk capital, is the owners' stake and bears the ultimate risk of the business. Any losses incurred directly reduce the owners' capital. In contrast, loans from creditors are fixed obligations that must be repaid in full, regardless of the business's profitability. Creditors' claims have priority over owners' claims.

May/June 2025

56. According to the business entity concept, if a firm earns a profit of ₹5,000, what is the dual effect on the accounting equation?

(A) Assets increase by ₹5,000, and liabilities to external creditors decrease by ₹5,000.

(B) Assets increase by ₹5,000, and owners' capital (a liability to owners) also increases by ₹5,000.

(C) Both assets and liabilities decrease by ₹5,000.

(D) There is no change in assets or liabilities, only in the P&L account.

Ans :

(B) Assets increase by ₹5,000, and owners' capital (a liability to owners) also increases by ₹5,000.

A profit of ₹5,000 typically results in an increase in assets (e.g., cash) by that amount. Since this profit belongs to the owners, the firm's liability to its owners (owners' capital) also increases by ₹5,000. This maintains the fundamental accounting equation where assets always equal liabilities plus owners' equity.

Oct/Nov 2019

57. What does a balance sheet represent?

(A) The summary of all transactions over an accounting period.

(B) A forecast of the company's financial performance for the next year.

(C) A photograph of the financial position (assets and liabilities) at a specific moment.

(D) A detailed breakdown of the company's operational expenses.

Ans :

(C) A photograph of the financial position (assets and liabilities) at a specific moment.

A balance sheet is a static report. It provides a snapshot of a company's financial health at a single point in time, showing what it owns (assets) and what it owes (liabilities and equity). It is not a record of transactions over a period but rather the cumulative result of all transactions up to that date.

May/June 2009

58. After all nominal accounts are transferred to the P&L account, which accounts are left in the General Ledger to form the balance sheet?

(A) Only Personal and Real accounts.

(B) Only Real accounts.

(C) Only Personal accounts.

(D) Only Nominal and Real accounts.

Ans :

(A) Only Personal and Real accounts.

The accounting process closes all temporary (Nominal) accounts, which are accounts for incomes and expenses, by transferring their balances to the P&L account. The remaining accounts in the General Ledger are the permanent accounts: Personal accounts (representing debtors, creditors, capital) and Real accounts (representing assets), which form the basis of the balance sheet.

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dividend accounts) to a permanent equity account (like Retained Earnings or Capital). This process zeroes out the temporary accounts and moves the net profit or loss into the P&L account.

Oct/Nov 2009

39. A Trading Account is primarily prepared to calculate which of the following?
(A) Net Profit
(B) Operating Profit
(C) Gross Profit
(D) Profit before Tax

Ans :

(C) Gross Profit
A trading account is a part of the P&L account that focuses on the direct costs and revenues associated with the goods being traded. It matches the sales revenue against the cost of goods sold to arrive at the Gross Profit or Gross Loss, which represents the profitability from the core buying and selling activities.

May/June 2023

40. What does the 'Cost of Goods Sold' (COGS) represent?
(A) The cost of only those goods which are sold during the year.
(B) The cost of all goods purchased during the year.
(C) The total operating expenses incurred to sell goods.
(D) The value of the closing inventory at the end of the year.

Ans :

(A) The cost of only those goods which are sold during the year.
The 'Cost of Goods Sold' is a crucial calculation that represents the direct costs attributable to the production or purchase of the goods that a company sold during a period. It does not include the cost of goods that were purchased but remain unsold in inventory at the end of the period.

Oct/Nov 2018

41. A firm has an opening stock of ₹1,000, purchases of ₹20,000, direct expenses of ₹500, and a closing stock of ₹8,000. What is the 'Cost of Goods Sold' (COGS)?
(A) ₹21,500
(B) ₹29,500
(C) ₹13,500
(D) ₹12,500

Ans :

(C) ₹13,500
The Cost of Goods Sold is calculated using the formula: COGS = (Opening Stock + Purchases + Direct Expenses) – Closing Stock . Substituting the given values: COGS = (₹1,000 + ₹20,000 + ₹500) – ₹8,000. This simplifies to ₹21,500 – ₹8,000, which equals ₹13,500. This is the cost of the goods sold during the period.

May/June 2007

42. Which of the following items would typically appear on the debit side of a traditional 'T-form' Trading Account?
(A) Sales and Closing Stock
(B) Opening Stock and Purchases
(C) Gross Loss and Sales
(D) Closing Stock and Gross Profit

Ans :

(B) Opening Stock and Purchases
In a standard T-account format for a Trading Account, the debit side includes all items related to the cost of goods available for sale. This comprises the Opening Stock, Purchases (net of returns), and all direct expenses like carriage inwards, wages, and freight. The resulting Gross Profit is also shown on the debit side to balance the account.

Oct/Nov 2025

43. In the vertical format of a Trading Account, how is Gross Profit calculated?
(A) Sales + Cost of Goods Sold
(B) Opening Stock + Purchases – Closing Stock
(C) Sales – Cost of Goods Sold
(D) Sales – (Opening Stock + Purchases)

Ans :

(C) Sales – Cost of Goods Sold
The vertical format presents the calculation in a statement form. It begins with the total Sales revenue for the period. From this, the Cost of Goods Sold (which is calculated as opening stock plus purchases and direct expenses, minus closing stock) is subtracted. The resulting figure is the Gross Profit for the period.

May/June 2012

44. What type of account is a 'Stock account'?
(A) A Personal account

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(B) A Nominal account
(C) A Fictitious account
(D) A Real account

Ans :

(D) A Real account
A stock account represents inventory, which is a tangible asset owned by the business. Accounts related to tangible and intangible assets are classified as Real accounts. Unlike nominal accounts, which are closed at year-end, the balance in a real account is carried forward to the next accounting period on the balance sheet.

Oct/Nov 2014

45. What is the accounting entry passed at the end of the year to record the value of closing stock in the books?
(A) Debit Stocks account and Credit Trading account.
(B) Debit Trading account and Credit Stocks account.
(C) Debit P&L account and Credit Stocks account.
(D) Debit Stocks account and Credit Purchases account.

Ans :

(A) Debit Stocks account and Credit Trading account.
At the end of the year, closing stock is an asset. To bring it into the books, the Stocks account (an asset account) is debited. This amount is then shown on the credit side of the Trading Account to correctly calculate the cost of goods sold and gross profit for the period.

May/June 2019

46. In the example where purchases were ₹20,000 and sales were ₹16,000, what were the total debits in the Purchase Account and total credits in the Sales account respectively?
(A) ₹16,000 and ₹20,000
(B) ₹20,000 and ₹16,000
(C) ₹20,000 and ₹20,500
(D) ₹16,000 and ₹16,000

Ans :

(B) ₹20,000 and ₹16,000
The Purchase Account is an expense-related account where purchases are recorded as debits. Therefore, its total debits would be ₹20,000. The Sales Account is a revenue account where sales are recorded as credits. Hence, its total credits would be ₹16,000. These are the primary entries before any returns are considered.

Oct/Nov 2006

47. Based on the provided Trading Account for the year ended 31-3-2022, what is the amount of Gross Profit?
(A) ₹11,000
(B) ₹16,000
(C) ₹8,000
(D) ₹2,500

Ans :

(D) ₹2,500
The Trading Account shows total credits (Sales ₹16,000 + Closing Stock ₹8,000) of ₹24,000. The total debits before profit are (Opening Stock ₹1,000 + Purchases ₹20,000 + Expenses ₹500) = ₹21,500. The balancing figure, which is the Gross Profit, is ₹24,000 - ₹21,500 = ₹2,500.

May/June 2021

48. For companies registered under the Companies Act 2013, how is the format for preparing the Profit and Loss account determined?
(A) The format is prescribed in the Act itself.
(B) It is not prescribed and is left to the discretion of the management.
(C) The format is determined by the Institute of Chartered Accountants of India.
(D) The format follows international best practices without any specific mandate.

Ans :

(A) The format is prescribed in the Act itself.
The Companies Act 2013 provides a specific, mandatory format for the preparation of financial statements, including the Statement of Profit and Loss, for all companies registered under it. This ensures uniformity and comparability. Similarly, banks and financial institutions must follow formats prescribed under the Banking Regulation Act or other relevant acts.

Oct/Nov 2010

49. If a Trading Account is prepared separately, how does the Profit and Loss Account typically begin?
(A) With the total sales figure for the year.
(B) With the opening stock value.
(C) With the Gross Profit or Gross Loss carried over from the Trading Account.
(D) With the total operating expenses for the

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year.

Ans :

(C) With the Gross Profit or Gross Loss carried over from the Trading Account.
When a Trading Account is used, it calculates the gross profit. This gross profit figure is then transferred to the credit side of the Profit and Loss Account (or gross loss to the debit side). The P&L account then continues by incorporating all indirect incomes and expenses to arrive at the net profit.

May/June 2005

50. If the practice of preparing a Trading Account is not followed, which item would appear in the combined Profit and Loss Account that is normally part of a separate Trading Account?
(A) Carriage Inwards
(B) Net Profit
(C) Depreciation
(D) Salary

Ans :

(A) Carriage Inwards
If a single, combined P&L account is prepared, it must include all items. This means direct costs and revenues, normally found in a Trading Account, are listed alongside indirect costs and revenues. Carriage inwards is a direct expense related to purchases and would therefore be included, unlike indirect expenses like salary or depreciation.

Oct/Nov 2022

51. What is the primary function of a Profit and Loss Appropriation account?
(A) To calculate the gross profit from trading activities.
(B) To record all cash and credit sales made during the year.
(C) To determine the cost of goods sold.
(D) To show the utilisation of net profit for dividends, reserves, and taxes.

Ans :

(D) To show the utilisation of net profit for dividends, reserves, and taxes.
The P&L Appropriation account is prepared after the net profit has been calculated. Its purpose is not to determine profit but to show how that profit is allocated or appropriated. This includes distributions like dividends to shareholders, transfers to various reserves, and provisions for taxes, showing the final surplus carried forward.

May/June 2018

52. Which of the following items would typically appear on the credit side of a Profit and Loss Appropriation account?
(A) Transfer to general reserve.
(B) Net profit for the year.
(C) Proposed dividend.
(D) Dividend Distribution Tax.

Ans :

(B) Net profit for the year.
The P&L Appropriation account starts with the profits available for distribution. The primary source of this is the net profit for the current year, which is transferred from the P&L account and shown on the credit side. Other credit items include the previous year's unappropriated profit and any amounts written back from reserves.

Oct/Nov 2016

53. Which of the following represents an appropriation of profit and would be debited to the P&L Appropriation account?
(A) Amount withdrawn from general reserve.
(B) Excess income tax provision written back.
(C) Transfer to debenture redemption reserve.
(D) Balance of surplus brought forward from the previous year.

Ans :

(C) Transfer to debenture redemption reserve.
The debit side of the P&L Appropriation account shows the uses or allocations of the available profit. Transferring a portion of the profit to a specific reserve, such as the debenture redemption reserve, is a common appropriation. This earmarks profits for a specific purpose and reduces the surplus available for distribution as dividends.

May/June 2014

54. According to Ind AS-1, what statement is prescribed instead of the traditional Profit and Loss Appropriation Account?
(A) Statement of Retained Earnings
(B) Statement of Comprehensive Income
(C) Statement of Financial Position
(D) Statement of Changes in Equity

Ans :

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This is an application of the principle of conservatism or prudence in accounting. This principle dictates that potential losses should be recognized, but potential gains should not be anticipated. By valuing stock at the lower of its cost or market value, the financial statements avoid overstating assets and profits, presenting a more cautious financial view.

May/June 2011

34. Under the FIFO method of inventory valuation, the material left in the godown as closing stock is assumed to be from which purchases?
(A) The material that was received first.
(B) An average of all materials received during the period.
(C) The material with the lowest purchase cost.
(D) The material that was received last.

Ans :

(D) The material that was received last.
The First-In, First-Out (FIFO) method assumes that the first items purchased are the first ones to be sold or used. Consequently, the inventory remaining at the end of the period (closing stock) is presumed to consist of the items that were purchased most recently. Therefore, its cost is based on the latest purchases.

Oct/Nov 2020

35. Which inventory valuation method assumes that the material last received in the godown is issued first?
(A) LIFO (Last-In, First-Out)
(B) FIFO (First-In, First-Out)
(C) Weighted Average Cost
(D) Specific Identification

Ans :

(A) LIFO (Last-In, First-Out)
The Last-In, First-Out (LIFO) method operates on the assumption that the most recently purchased items are the first ones to be sold. As a result, the closing inventory is valued based on the cost of the earliest purchases. The cost of goods sold under LIFO reflects the most recent costs.

May/June 2022

36. Which inventory valuation methods are permitted for use under Indian Accounting Standard (Ind AS 2)?
(A) Only FIFO method.
(B) FIFO or the Weighted Average method.
(C) Only LIFO method.
(D) Only Weighted Average method.

Ans :

(B) FIFO or the Weighted Average method.
Indian Accounting Standard (Ind AS 2) on Inventories provides specific guidance on valuation methods. It explicitly permits the use of either the First-In, First-Out (FIFO) method or the Weighted Average Cost method. The standard does not permit the use of the Last-In, First-Out (LIFO) method for inventory valuation for entities following Ind AS.

Oct/Nov 2023

37. Which of the following is an example of an adjustment for "Other Items" mentioned in the preparation of final accounts?
(A) Recording sales revenue for the year.
(B) Paying monthly rent for the office premises.
(C) Purchasing raw materials on cash.
(D) Making a provision for bad and doubtful debts.

Ans :

(D) Making a provision for bad and doubtful debts.
Adjustments for "Other Items" typically refer to non-operational or valuation adjustments made at year-end. Making a provision for bad and doubtful debts is a classic example, as it involves estimating potential losses from receivables and is not a direct result of a day-to-day purchase or sale transaction.

May/June 2016

38. What is the purpose of passing "closing entries" at the end of an accounting period?
(A) To transfer the balances of all income and expense accounts to the P&L account.
(B) To close the asset and liability accounts and transfer them to the P&L account.
(C) To create opening balances for the next accounting period.
(D) To reconcile the bank statement with the cash book.

Ans :

(A) To transfer the balances of all income and expense accounts to the P&L account.
Closing entries are journal entries made at the end of an accounting period to transfer the balances of temporary accounts (income, expense, and

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Oct/Nov 2011

59. If a machine is purchased for ₹5,000 by using cash, what is the immediate effect on the balance sheet?
(A) Total assets increase by ₹5,000.
(B) Total assets decrease by ₹5,000.
(C) Total assets remain the same, but their composition changes.
(D) Total liabilities increase by ₹5,000.

Ans :

(C) Total assets remain the same, but their composition changes.
This transaction is an exchange of one asset for another. The cash balance (an asset) decreases by ₹5,000, while fixed assets (machinery) increase by ₹5,000. The net effect on the total value of assets is zero. The composition of the assets simply shifts from cash to a non-current asset.

May/June 2010

60. In the simplified vertical format of a balance sheet provided, which of the following is NOT listed under the 'Assets' category?
(A) Capital.
(B) Non-current Assets
(C) Cash
(D) Stocks

Ans :

(A) Capital.
Capital represents the investment made by the owners in the business. From the business entity's perspective, this is an amount owed to the owners and is therefore classified as a liability (specifically, owner's equity). Assets are resources owned by the business, such as non-current assets, cash, stocks, and receivables.

Oct/Nov 2024

61. Which of the following is a key characteristic of the "Statement of changes in equity" as prescribed by Ind AS-1?
(A) It is an optional statement for companies to prepare.
(B) It is identical in content to the P&L Appropriation Account.
(C) It only shows the net profit or loss for the period.
(D) It incorporates transactions with owners in their capacity as owners.

Ans :

(D) It incorporates transactions with owners in their capacity as owners.
The "Statement of changes in equity" is a more detailed and comprehensive statement than the traditional P&L Appropriation Account. A key feature is that it includes not just profit appropriations but also changes in equity arising from transactions with owners, such as the issuance of new share capital or share buybacks.

May/June 2017

62. Which of the following pairs is correctly matched?
(A) Amortisation - Tangible Assets
(B) Accrual Basis - Mandated by AS-1
(C) Ind AS 16 - Intangible Assets
(D) LIFO Method - Permitted by Ind AS 2

Ans :

(B) Accrual Basis - Mandated by AS-1
AS-1 states that accrual is a fundamental accounting assumption, mandating its use. Amortisation relates to intangible assets. Ind AS 16 deals with tangible assets (Property, Plant, and Equipment). The LIFO method is not permitted under Ind AS 2.

Oct/Nov 2005

63. Identify the incorrect statement regarding the preparation of final accounts.
(A) A trial balance is not a financial statement.
(B) Depreciation is a non-cash but actual expense.
(C) Closing stock is valued at the higher of cost or market value.
(D) The P&L Appropriation account shows the distribution of net profit.

Ans :

(C) Closing stock is valued at the higher of cost or market value.
The principle of conservatism dictates that inventory (closing stock) should be valued at the lower of its purchase cost or net realizable (market) value. This practice prevents the overstatement of assets and profits. Stating that it is valued at the higher of the two is incorrect and violates this fundamental accounting principle.

May/June 2020

64. Consider the following statements:
1. All ledger accounts are balanced and a trial balance is prepared at the end of the accounting year.

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2. The trial balance itself is a formal financial statement presented to stakeholders.

Which of the statements is/are correct?
(A) Only 1
(B) Only 2
(C) Both 1 and 2
(D) Neither 1 nor 2

Ans :

(A) Only 1
Statement 1 is correct; it describes the standard procedure at the end of an accounting year before preparing final accounts. Statement 2 is incorrect; a trial balance is an internal worksheet used to verify debit-credit equality and is not a formal financial statement intended for external stakeholders like the balance sheet or P&L account.

Oct/Nov 2015

65. Consider the following statements about depreciation:
1. Depreciation is charged on all fixed assets including land.
2. It is a cash expense paid annually for asset maintenance.
3. It is a book entry that does not affect the cash account.

Which of the statements is/are correct?
(A) Only 3
(B) Only 1 and 2
(C) Only 2 and 3
(D) All 1, 2 and 3

Ans :

(A) Only 3
Statement 3 is correct; depreciation is a non-cash charge. Statement 1 is incorrect because land is generally not depreciated. Statement 2 is incorrect because depreciation is a non-cash expense representing the consumption of an asset's value, not a cash payment for maintenance. Therefore, only the third statement is accurate.

May/June 2013

66. Match List-I (Accounting Concept) with List-II (Description).
List-I
P. Accrued Income
Q. Prepaid Expense
R. Outstanding Expense
S. Unearned Income
List-II
1. Expense incurred but not yet paid.
2. Income received but not yet earned.
3. Income earned but not yet received.
4. Expense paid in advance but not yet incurred.

(A) P-3, Q-4, R-1, S-2
(B) P-4, Q-3, R-2, S-1
(C) P-3, Q-1, R-4, S-2
(D) P-2, Q-4, R-1, S-3

Ans :

(A) P-3, Q-4, R-1, S-2
P. Accrued Income is income earned but not received (3). Q. Prepaid Expense is an expense paid in advance (4). R. Outstanding Expense is an expense incurred but not paid (1). S. Unearned Income is income received in advance but not yet earned (2). The correct matching reflects these standard accounting definitions.

Oct/Nov 2021

67. Which of the following is the correct formula for Cost of Goods Sold (COGS)?
(A) Sales – Gross Profit
(B) Opening Stock + Purchases – Sales
(C) Purchases + Closing Stock – Opening Stock
(D) (Opening Stock + Purchases + Expenses) – Closing Stock

Ans :

(D) (Opening Stock + Purchases + Expenses) – Closing Stock
The cost of goods sold represents the cost of inventory that was sold during a period. It is calculated by taking the value of the opening stock, adding all purchases and direct expenses made during the period, and then subtracting the value of the stock that remains unsold at the end of the period (closing stock).

May/June 2024

68. Which of the following statements about inventory valuation is/are correct?
1. The LIFO method is permitted under Ind AS 2.
2. The FIFO method assumes the first goods purchased are the first to be sold.
3. An undervaluation of closing stock will result in understating the profits.

(A) Only 1 and 2
(B) Only 2 and 3
(C) Only 1 and 3
(D) All 1, 2 and 3

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Ans :

(B) Only 2 and 3
Statement 1 is incorrect; Ind AS 2 does not permit the LIFO method. Statement 2 is a correct definition of the FIFO method. Statement 3 is correct; if closing stock (a deduction from costs) is undervalued, the cost of goods sold will be higher, which in turn leads to an understatement of profits.

Oct/Nov 2008

69. Which of the following items are NOT part of a Trading Account?
1. Salary
2. Carriage Inwards
3. Depreciation
4. Sales

(A) 1 and 3
(B) 2 and 4
(C) 1, 2 and 3
(D) 2, 3 and 4

Ans :

(A) 1 and 3
A Trading Account includes only direct revenues and direct expenses related to the goods being traded. Sales (4) is the direct revenue and Carriage Inwards (2) is a direct expense. Salary (1) and Depreciation (3) are indirect (operating) expenses and are therefore shown in the Profit and Loss Account, not the Trading Account.

May/June 2006

70. **Assertion (A) :** The balance in the Stock Account remains unchanged throughout the year until the closing stock is valued.
Reason (R) : Entries for purchases and sales are posted to the Purchase Account and Sales Account, not the Stock Account.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is true; the stock account reflects the opening balance all year. Reason (R) is also true and correctly explains why this happens in a periodic inventory system. Since day-to-day purchases and sales transactions are recorded in separate nominal accounts (Purchases and Sales), the Stock (asset) account is not affected until the year-end adjustment.

Oct/Nov 2017

71. Identify the correct pair of accounting standards and their subject matter.
(A) Ind AS 16: Intangible Assets
(B) Ind AS 38: Depreciation of Tangible Assets
(C) AS-26: Inventories
(D) AS-10: Property, Plant and Equipment

Ans :

(D) AS-10: Property, Plant and Equipment
AS-10 correctly corresponds to Property, Plant and Equipment (tangible fixed assets). Ind AS 16 deals with tangible assets, not intangible. Ind AS 38 deals with intangible assets, not depreciation of tangible assets. AS-26 deals with intangible assets, not inventories (which is AS-2).

May/June 2008

72. Which of the following items would cause the debit side of the P&L Appropriation Account to increase?
(A) Net Profit for the year
(B) Interim Dividend declared and paid
(C) Amount withdrawn from general reserve
(D) Excess income tax provision written back

Ans :

(B) Interim Dividend declared and paid
The debit side of the P&L Appropriation Account reflects the uses or allocations of profit. Declaring and paying an interim dividend is a distribution of profit to shareholders, and therefore it is debited to this account. The other options are all items that would appear on the credit side, as they represent profits available for appropriation.

Oct/Nov 2013

73. Consider the following statements regarding the Balance Sheet:
1. It is a statement of assets and liabilities at a particular moment.
2. The total of assets must always equal the total of liabilities and owner's equity.
3. It includes nominal, real, and personal accounts.

Which of the above statements are correct?
(A) 1 and 2 only

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(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2 and 3

Ans :

(A) 1 and 2 only
Statements 1 and 2 are fundamental truths about the balance sheet. It is a snapshot in time (1) and must always balance based on the accounting equation (2). Statement 3 is incorrect because nominal accounts (income/expenses) are closed to the P&L account and do not appear directly on the balance sheet.

May/June 2015

74. Which of the following is an INCORRECT statement?
(A) A Trading Account is a necessary step for the preparation of the P&L account.
(B) Closing entries are passed to make the balances in income and expense accounts Nil.
(C) A business entity is considered separate from its promoters for accounting purposes.
(D) Profit earned by a firm results in an increase in both assets and owners' capital.

Ans :

(A) A Trading Account is a necessary step for the preparation of the P&L account.
The preparation of a Trading Account is a common practice but is not a mandatory or necessary step. Accountants can choose to prepare a single, combined Profit and Loss Account that incorporates all direct and indirect incomes and expenses to arrive at the net profit, bypassing the intermediate step of calculating gross profit.

Oct/Nov 2012

75. If the opening stock is ₹9,000, purchases are ₹1,70,000, and sales are ₹2,00,000, what additional information is essential to calculate the Cost of Goods Sold?
(A) The amount of operating expenses.
(B) The amount of cash received from sales.
(C) The value of the closing stock.
(D) The net profit for the year.

Ans :

(C) The value of the closing stock.
The Cost of Goods Sold (COGS) is calculated as Opening Stock + Purchases - Closing Stock (assuming no direct expenses). Without knowing the value of the inventory remaining at the end of the period (closing stock), it is impossible to determine the cost of the specific goods that were actually sold during that period.

May/June 2011

76. "The Accounting Standard (AS-1) states that accrual is a fundamental accounting assumption. The Indian Accounting Standard (Ind AS-1) also requires that an entity shall prepare its financial statements, except for cash flow information, using the accrual basis of accounting."
Based on this excerpt, for which financial statement is the accrual basis of accounting NOT a requirement?
(A) Profit and Loss Account
(B) Statement of Cash Flows
(C) Balance Sheet
(D) Statement of Changes in Equity

Ans :

(B) Statement of Cash Flows
The provided text explicitly mentions an exception to the accrual basis requirement. It states that an entity shall prepare its financial statements using the accrual basis, with the specific exclusion of "cash flow information". The Statement of Cash Flows is prepared on a cash basis to show the movement of cash and cash equivalents.

Oct/Nov 2020

77. "Depreciation is an actual expense, though not a cash expense of the business. Therefore, before preparing the P&L account of the firm, we should calculate the depreciation amount and debit it to expenses account. Which account will be credited? Obviously, the fixed assets account."
According to the source, what is the impact of the credit entry for depreciation?
(A) It increases the cash balance of the firm.
(B) It increases the total expenses shown in the P&L account.
(C) It creates a provision for replacing the asset in the future.
(D) It reduces the existing debit balance in the fixed assets account.

Ans :

(D) It reduces the existing debit balance in the fixed assets account.
The source states that the fixed assets account will be credited. Since fixed assets are assets, they normally have a debit balance. A credit

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entry to an asset account results in a reduction of its balance. Therefore, the credit part of the depreciation entry signifies a reduction in the book value of the fixed asset.

May/June 2022

78. "The accounting principles tell us that we should take the lower of the purchase cost or market value for the closing stock."
What is the primary objective of applying this valuation principle for closing stock?
(A) To ensure that assets and profits are not overstated in the financial statements.
(B) To maximize the reported profit for the accounting period.
(C) To simplify the calculation of the cost of goods sold.
(D) To align the inventory value with its future replacement cost.

Ans :

(A) To ensure that assets and profits are not overstated in the financial statements.
The principle of valuing inventory at the lower of cost or market value is an application of conservatism. By choosing the lower value, a company ensures it does not recognize unrealized gains and accounts for potential losses if the market value has fallen below cost. This prevents the overstatement of both assets and profits.

Oct/Nov 2023

79. "Indian Accounting Standard (Ind AS 2) permits use of only FIFO or the Weighted Average Method for valuation of inventories."
A company follows Ind AS for its financial reporting. It has been using the LIFO method for inventory valuation. What must the company do to comply with Ind AS 2?
(A) Continue using the LIFO method as it is a widely recognized method.
(B) Apply for a special exemption from the standard to continue using LIFO.
(C) Switch to either the FIFO or the Weighted Average method.
(D) Use a combination of LIFO and FIFO for different categories of inventory.

Ans :

(C) Switch to either the FIFO or the Weighted Average method.
The source text is unequivocal in stating that Ind AS 2 permits only two methods: FIFO and Weighted Average. Therefore, a company that is required to comply with Ind AS and is currently using the LIFO method must change its accounting policy and adopt one of the two permitted methods to be in compliance.

May/June 2016

80. "Cost of Goods Sold = (opening stock + purchases + expenses) – (closing stock)"
Using the provided formula, if a company's sales are ₹50,000, opening stock is ₹5,000, purchases are ₹30,000, direct expenses are ₹2,000 and closing stock is ₹7,000, what is the Gross Profit?
(A) ₹20,000
(B) ₹30,000
(C) ₹24,000
(D) ₹26,000

Ans :

(A) ₹20,000
First, calculate the Cost of Goods Sold (COGS) using the formula: COGS = (opening stock + purchases + expenses) – (closing stock) . COGS = (₹5,000 + ₹30,000 + ₹2,000) – ₹7,000 = ₹30,000. Gross Profit is calculated as Sales – COGS. Therefore, Gross Profit = ₹50,000 – ₹30,000 = ₹20,000. The calculation directly applies the provided formula and the definition of gross profit.

Oct/Nov 2009

81. "The balance in this newly opened P&L account, along with the balances in all the remaining accounts in the GL, forms part of the balance sheet... So, only Personal and Real accounts are left in the General Ledger and these, along with net profit/loss, form the balance sheet."
Based on this text, what happens to nominal accounts at year-end?
(A) They are carried forward to the next year's balance sheet.
(B) They are merged with personal accounts to simplify the balance sheet.
(C) They are directly closed and transferred to the Capital account.
(D) Their balances are transferred to the P&L account and are not part of the balance sheet.

Ans :

(D) Their balances are transferred to the P&L account and are not part of the balance sheet.
The excerpt clearly states that only Personal and Real accounts, along with the P&L summary (net

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(B) The gross profit earned on the stock.
(C) The value of closing stock which becomes the opening stock for the next year.
(D) The value of stock at the beginning of the year.

Ans :

(C) The value of closing stock which becomes the opening stock for the next year.
The entry 'By closing balance carried forward' on the credit side of the Stocks account represents the value of the inventory at the end of the accounting period. This balance is carried over to the next financial year, where it will appear on the debit side as 'To opening balance brought forward'.

May/June 2009

100. If a P&L Account starts with "By Gross profit carried over from Trading a/c," what kind of expenses would be debited to this P&L account?
(A) Indirect expenses like salary, rent, and depreciation.
(B) Direct expenses like wages and freight.
(C) All expenses, both direct and indirect.
(D) Only non-cash expenses like depreciation.

Ans :

(A) Indirect expenses like salary, rent, and depreciation.
When a separate Trading Account is prepared, it has already accounted for all direct expenses to calculate the gross profit. The Profit and Loss Account then starts with this gross profit and deducts all indirect (or operating) expenses, such as administrative, selling, and financial expenses, to arrive at the net profit.

Oct/Nov 2011

101. A company has a net profit of ₹5,00,000. The board decides to transfer ₹1,00,000 to the general reserve and propose a dividend of ₹2,00,000. Where are these transactions recorded?
(A) In the Trading Account.
(B) In the Profit and Loss Account.
(C) Directly in the Balance Sheet.
(D) In the Profit and Loss Appropriation Account.

Ans :

(D) In the Profit and Loss Appropriation Account.
The transfer to reserves and the proposal of a dividend are not operating expenses incurred to earn profit; they are allocations of the profit after it has been earned. Such appropriations of profit are recorded in the Profit and Loss Appropriation Account, which shows how the net profit is utilized by the company.

May/June 2010

102. Which of the following would be an incorrect entry in a P&L Appropriation Account?
(A) Debit to 'Transfer to general reserve'.
(B) Debit to 'Purchase of fixed assets'.
(C) Credit to 'Net Profit for the year'.
(D) Debit to 'Proposed dividend'.

Ans :

(B) Debit to 'Purchase of fixed assets'.
The purchase of a fixed asset is a capital expenditure that affects the Balance Sheet (increasing assets and decreasing cash or increasing liabilities). It is not an appropriation of profit. The P&L Appropriation account deals exclusively with the allocation of net profit to reserves, dividends, and taxes, not with asset acquisition.

Oct/Nov 2024

103. When a partnership firm ABC starts with an induction of capital of ₹50,000, what is the accounting entry?
(A) Debit Capital ₹50,000; Credit Cash ₹50,000
(B) Debit P&L Account ₹50,000; Credit Capital ₹50,000
(C) Debit Cash ₹50,000; Credit Capital ₹50,000
(D) Debit Capital ₹50,000; Credit Bank Loan ₹50,000

Ans :

(C) Debit Cash ₹50,000; Credit Capital ₹50,000
When capital is introduced, the firm's cash (an asset) increases. Therefore, the Cash account is debited. This investment creates a liability for the firm towards its owners (promoters), which is represented by the Capital account. Therefore, the Capital account is credited. This entry reflects the increase in assets and corresponding increase in equity.

May/June 2017

104. The balance sheet of ABC Ltd. as on 31-3-2021 shows total liabilities of ₹80,000. What must be the total of its assets on the same date?
(A) ₹50,000
(B) ₹30,000
(C) Cannot be determined from the given

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May/June 2012

86. Case: A young entrepreneur invested ₹10 lacs in computer systems for a cyber café. During the first year, total receipts were ₹5 lacs and total payments (rent, salary, etc.) were ₹3 lacs. He did not account for depreciation.
What was the cash surplus for the first year, and how does it differ from the actual profit?
(A) Cash surplus was ₹2 lacs, which is the actual profit.
(B) Cash surplus was ₹2 lacs, but actual profit is lower due to unrecorded depreciation expense.
(C) Cash surplus was ₹8 lacs, and the actual profit is also ₹8 lacs.
(D) Cash surplus was ₹5 lacs, but the actual profit cannot be determined.

Ans :

(B) Cash surplus was ₹2 lacs, but actual profit is lower due to unrecorded depreciation expense.
The cash surplus is the difference between cash receipts (₹5 lacs) and cash payments (₹3 lacs), which is ₹2 lacs. However, this is not the actual profit. The computer systems (a fixed asset) lose value over time due to use and obsolescence. This non-cash expense, depreciation, must be deducted to arrive at the actual, lower profit figure.

Oct/Nov 2014

87. Case: After 4 years, the entrepreneur's cyber café systems, which cost ₹10 lacs, could be sold for only ₹2 lacs. Over the 4 years, he had accumulated a total cash surplus of ₹8 lacs.
Considering the asset's loss in value, what was the total economic outcome of the business over the four years?
(A) A total profit of ₹8 lacs.
(B) A total profit of ₹6 lacs.
(C) A total loss of ₹2 lacs.
(D) A break-even with zero profit or loss.

Ans :

(D) A break-even with zero profit or loss.
The total cash generated (surplus) was ₹8 lacs. The economic cost of using the computer systems is their decline in value, which is the initial cost minus the disposal value (₹10 lacs - ₹2 lacs = ₹8 lacs). The actual overall profit is cash surplus minus this economic cost (₹8 lacs - ₹8 lacs = ₹0).

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May/June 2019

88. Case: A company's records for the year ended 31-3-2022 show: Opening Stock ₹9,000; Purchases ₹1,70,000; Expenses ₹20,000; Sales ₹2,00,000; Closing Stock ₹10,000.
Based on the P&L account provided in the chapter's illustration, what is the Net Profit for the year ended 31-3-2022?
(A) ₹11,000
(B) ₹21,000
(C) ₹1,000
(D) ₹9,000

Ans :

(A) ₹11,000
The net profit is calculated by finding the difference between the credit and debit sides of the P&L account. Total credits = Sales (₹2,00,000) + Closing Stock (₹10,000) = ₹2,10,000. Total debits (before profit) = Opening Stock (₹9,000) + Purchases (₹1,70,000) + Expenses (₹20,000) = ₹1,99,000. Net Profit = ₹2,10,000 - ₹1,99,000 = ₹11,000.

Oct/Nov 2006

89. Case: ABC Ltd.'s balance sheet on 31-3-2021 showed Capital of ₹50,000. During the year 2021-22, the company earned a net profit of ₹11,000. There were no other transactions affecting capital.
What would be the closing balance of the Capital account as on 31-3-2022?
(A) ₹50,000
(B) ₹39,000
(C) ₹61,000
(D) ₹11,000

Ans :

(C) ₹61,000
The closing balance of the Capital account is calculated by taking the opening balance and adding the net profit for the period (assuming no drawings or fresh capital infusion). Therefore, the closing capital would be the opening balance of ₹50,000 plus the net profit of ₹11,000, resulting in a total of ₹61,000.

May/June 2021

90. Case: ABC Ltd. had an opening cash balance of ₹15,000. During the year, cash receipts from sales/receivables were ₹1,98,000. Cash payments were: Fixed assets ₹10,000, Purchases ₹1,70,000,

machinery.
Statement II : Ind AS 38 provides guidelines for the amortisation of intangible assets.
(A) Statement I is correct, but Statement II is incorrect.
(B) Statement II is correct, but Statement I is incorrect.
(C) Both Statement I and Statement II are correct.
(D) Both Statement I and Statement II are incorrect.

Ans :

(B) Statement II is correct, but Statement I is incorrect.
Statement II is correct; Ind AS 38 is the standard for intangible assets and their amortisation. Statement I is incorrect because amortisation applies to intangible assets. The process of writing off the value of tangible fixed assets like machinery is called depreciation, which is covered under Ind AS 16.

May/June 2024

110. What is the logical sequence of the following accounting activities?
1. Preparation of Trial Balance
2. Preparation of Balance Sheet
3. Passing of Adjustment Entries
4. Preparation of P&L Account

(A) 1, 3, 4, 2
(B) 1, 4, 3, 2
(C) 3, 1, 4, 2
(D) 2, 1, 3, 4

Ans :

(A) 1, 3, 4, 2
The correct sequence is: First, a trial balance is prepared from ledger balances (1). Second, adjustment entries are passed to account for accruals and prepayments (3). Third, the adjusted balances are used to prepare the P&L Account to find the net profit/loss (4). Finally, the Balance Sheet is prepared using the remaining asset, liability, and equity balances (2).

Oct/Nov 2008

111. Which of the following methods of inventory valuation is based on the assumption that the cost of closing stock consists of the earliest purchase costs?
(A) FIFO Method
(B) Weighted Average Cost Method
(C) Market Value Method
(D) LIFO Method

Ans :

(D) LIFO Method
The Last-In, First-Out (LIFO) method assumes that the most recently purchased items are sold first. Therefore, the items remaining in inventory (closing stock) are assumed to be the ones that were purchased earliest. Consequently, the closing stock is valued at the cost of the first or earliest materials acquired.

May/June 2006

112. Which of the following is NOT an appropriation of profit and hence, would not appear on the debit side of a P&L Appropriation Account?
(A) Transfer to general reserve
(B) Provision for bad and doubtful debts
(C) Proposed dividend
(D) Income tax for previous years not provided for

Ans :

(B) Provision for bad and doubtful debts
Provision for bad and doubtful debts is a charge against profit, not an appropriation of it. It is an estimated business expense required to state the receivables at their net realizable value and is debited to the P&L account itself. The other items are all examples of how net profit is allocated or used.

Oct/Nov 2017

113. A company takes a loan of ₹30,000 from Mr. A. What is the effect of this transaction on the company's balance sheet?
(A) Assets decrease by ₹30,000 and Liabilities decrease by ₹30,000.
(B) Assets increase by ₹30,000 and Capital increases by ₹30,000.
(C) Assets increase by ₹30,000 and Liabilities increase by ₹30,000.
(D) No change in the balance sheet total.

Ans :

(C) Assets increase by ₹30,000 and Liabilities increase by ₹30,000.
When the company receives the loan, its cash (an asset) increases by ₹30,000. Simultaneously, it incurs an obligation to repay Mr. A, which is a liability. Therefore, the loans (a liability) also increase by ₹30,000. This transaction increases

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To adhere to the accrual concept, the rent expense for all 12 months must be shown in the P&L account. An adjustment is needed for the unpaid March rent. The 'Rent Paid' account is debited to increase the total rent expense to ₹60,000. A liability account, 'Rent Payable', is credited to reflect the obligation.

Oct/Nov 2016

95. Case: A company receives ₹12,000 from a tenant on March 15th as rent for the months of March, April, and May (₹4,000 per month). The financial year ends on March 31st.
How much of the ₹12,000 should be recognized as income for the current financial year?
(A) ₹4,000
(B) ₹12,000
(C) ₹8,000
(D) ₹0

Ans :

(A) ₹4,000
According to the accrual principle, income should be recognized only when it is earned. Of the three months' rent received, only the rent for March has been earned within the current financial year. The rent for April and May (₹8,000) is considered 'Unearned Income' and will be recognized as income in the next financial year.

May/June 2014

96. The balance in the 'Salary account' of a firm is ₹3,00,000. To close this account at year-end, a credit entry 'By transfer to P&L account' is posted. What is the corresponding debit entry?
(A) A debit entry will be posted to the 'Cash' account.
(B) A debit entry will be posted to the P&L account.
(C) A debit entry will be posted to the 'Salary Payable' account.
(D) A debit entry will be posted to the 'Capital' account.

Ans :

(B) A debit entry will be posted to the P&L account.
This is a closing entry. The purpose is to transfer the balance of the nominal account (Salary) to the Profit and Loss account. Crediting the Salary account makes its balance nil. To complete the double entry, the Profit and Loss account is debited, reflecting the salary as an expense for the period.

Oct/Nov 2007

97. In the context of the Trading Account format, which of the following is considered a direct expense associated with purchases?
(A) Office Salaries
(B) Depreciation of Office Furniture
(C) Advertisement Expenses
(D) Carriage inwards

Ans :

(D) Carriage inwards
Direct expenses are costs incurred to bring goods to a saleable condition or location. 'Carriage inwards' refers to the transportation costs for bringing purchased goods into the business, so it is a direct expense included in the Trading Account. Salaries, depreciation, and advertising are indirect or operating expenses shown in the P&L Account.

May/June 2025

98. The vertical format for a Trading Account is presented as: Sales (A) - Cost of Goods Sold (B) = Gross Profit (A-B). What does the component 'B' (Cost of Goods Sold) consist of?
(A) Purchases + Opening Stocks + Expenses - Closing Stocks
(B) Purchases + Opening Stocks + Expenses + Closing Stocks
(C) Purchases - Opening Stocks + Expenses + Closing Stocks
(D) Purchases + Opening Stocks - Expenses - Closing Stocks

Ans :

(A) Purchases + Opening Stocks + Expenses - Closing Stocks
The Cost of Goods Sold (COGS) represents the cost of inventory sold. It is calculated by adding the cost of opening inventory, purchases, and other direct expenses incurred during the period, and then subtracting the cost of inventory that is still on hand at the end of the period (closing stock).

Oct/Nov 2019

99. In the Stocks account ledger shown for the year 1-4-2021 to 31-3-2022, what does the entry 'By closing balance carried forward ₹8,000' represent?
(A) The value of stock sold during the year.

Long-term liabilities ₹5,000, Short-term liabilities ₹2,000, and Expenses ₹20,000.
What is the closing cash balance as on 31-3-2022?
(A) ₹6,000
(B) ₹15,000
(C) ₹21,000
(D) ₹8,000

Ans :

(A) ₹6,000
To find the closing cash balance, start with the opening balance, add all cash inflows, and subtract all cash outflows. Calculation: ₹15,000 (Opening) + ₹1,98,000 (Inflows) - ₹10,000 - ₹1,70,000 - ₹5,000 - ₹2,000 - ₹20,000 (Outflows) = ₹2,13,000 - ₹2,07,000 = ₹6,000. This is the final cash balance.

Oct/Nov 2010

91. Case: On 31-3-2021, ABC Ltd. had Long Term Liabilities of ₹20,000 and Short Term Liabilities of ₹10,000. During the year 2021-22, it made repayments of ₹5,000 towards long term loans and ₹2,000 towards short term loans.
What are the balances of Long Term and Short Term Liabilities on the 31-3-2022 balance sheet?
(A) Long Term ₹20,000; Short Term ₹10,000
(B) Long Term ₹25,000; Short Term ₹12,000
(C) Long Term ₹5,000; Short Term ₹2,000
(D) Long Term ₹15,000; Short Term ₹8,000

Ans :

(D) Long Term ₹15,000; Short Term ₹8,000
The closing balance of a liability is its opening balance minus any repayments made during the period. For Long Term Liabilities: ₹20,000 - ₹5,000 = ₹15,000. For Short Term Liabilities: ₹10,000 - ₹2,000 = ₹8,000. These are the new balances that will be reflected on the balance sheet as of 31-3-2022.

May/June 2005

92. Case: On 31-3-2021, ABC Ltd. had Non-current assets of ₹50,000. During the year 2021-22, the company purchased additional fixed assets worth ₹10,000. There were no sales of assets or depreciation entries made.
What is the value of Fixed assets on the balance sheet as on 31-3-2022?
(A) ₹50,000
(B) ₹60,000
(C) ₹40,000
(D) ₹10,000

Ans :

(B) ₹60,000
The closing balance of fixed assets is calculated by taking the opening balance and adding the cost of any new assets purchased during the period. Since there were no sales or depreciation, the calculation is simply: Opening Balance ₹50,000 + Purchase ₹10,000 = ₹60,000. This will be the value shown on the closing balance sheet.

Oct/Nov 2022

93. Case: Based on the final balance sheet of ABC Ltd. as on 31-3-2022, the total liabilities are: Capital ₹61,000, Long term liabilities ₹15,000, and Short term liabilities ₹8,000.
What should be the total value of assets on the same balance sheet?
(A) ₹61,000
(B) ₹23,000
(C) ₹84,000
(D) ₹94,000

Ans :

(C) ₹84,000
According to the fundamental accounting equation, Total Assets must equal Total Liabilities (including Capital/Equity). The total liabilities are the sum of Capital (₹61,000), Long term liabilities (₹15,000), and Short term liabilities (₹8,000). The sum is ₹61,000 + ₹15,000 + ₹8,000 = ₹84,000. Therefore, the total assets must also be ₹84,000.

May/June 2018

94. Case: A firm pays office rent of ₹5,000 per month. At the end of the financial year on March 31, the rent for March has not yet been paid. The 'Rent Paid' account in the trial balance shows a debit balance of ₹55,000 (for 11 months).
What adjustment entry is required to present a fair P&L account?
(A) Debit 'Rent Paid' ₹5,000; Credit 'Cash' ₹5,000
(B) Debit 'Rent Payable' ₹5,000; Credit 'Rent Paid' ₹5,000
(C) No entry is needed until the rent is actually paid.
(D) Debit 'Rent Paid' ₹5,000; Credit 'Rent Payable' ₹5,000

Ans :

(D) Debit 'Rent Paid' ₹5,000; Credit 'Rent Payable' ₹5,000

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information.
(D) ₹80,000

Ans :

(D) ₹80,000
A fundamental principle of accounting is that the balance sheet must always balance. This means that the total value of a company's assets must be equal to the total value of its liabilities plus owners' equity. If the total liabilities (including capital) are ₹80,000, then the total assets must also be ₹80,000.

Oct/Nov 2005

105. In the final balance sheet of ABC Ltd. as on 31-3-2022, the total is ₹84,000. Which figure represents the owner's equity component on that date?
(A) ₹61,000
(B) ₹84,000
(C) ₹15,000
(D) ₹8,000

Ans :

(A) ₹61,000
The balance sheet shows three components on the liabilities side: Capital, Long term liabilities, and Short term liabilities. Owner's equity is represented by the 'Capital' account. On the 31-3-2022 balance sheet, the amount shown against Capital is ₹61,000, which represents the owner's stake in the company on that date.

May/June 2020

106. Which of the following is NOT a primary objective of preparing final accounts as per the chapter's introduction?
(A) To show the profit earned or loss sustained by the business.
(B) To determine the market value of the company's shares.
(C) To provide a fair picture of the enterprise's operations to stakeholders.
(D) To show the final picture regarding its assets and liabilities.

Ans :

(B) To determine the market value of the company's shares.
Final accounts provide historical financial information about performance (profit/loss) and position (assets/liabilities). While this information is used by investors to make decisions, the accounts themselves do not determine the market value of shares. Share price is determined by market forces of supply and demand, influenced by many factors beyond the accounting statements.

Oct/Nov 2015

107. The process of preparing a trial balance has become less important for bookkeeping purposes due to accounting software. However, it remains important for which group of professionals?
(A) Customers and Suppliers
(B) Government Regulators
(C) Marketing and Sales staff
(D) Accountants and Auditors

Ans :

(D) Accountants and Auditors
While software ensures debit-credit equality, the trial balance is still a crucial document for accountants and auditors. It provides a consolidated view of all ledger balances before and after adjustments, which is essential for analysis, verification, and the audit process. It serves as the primary source for drafting the final financial statements.

May/June 2013

108. Identify the incorrect pair from the following adjustment entries.
(A) Advance Rent Received: Debit Cash A/c, Credit Advance Rent Received A/c
(B) Outstanding Salary: Debit Salary A/c, Credit Salary Payable A/c
(C) Prepaid Insurance: Debit Prepaid Insurance A/c, Credit Insurance A/c
(D) Accrued Interest Income: Debit Interest Receivable A/c, Credit Interest Income A/c

Ans :

(A) Advance Rent Received: Debit Cash A/c, Credit Advance Rent Received A/c
The adjustment for advance rent received aims to defer the income. The initial entry upon receipt of cash was Debit Cash, Credit Rent Received. The adjustment entry should be Debit 'Rent Received' A/c and Credit 'Advance Rent Received' A/c (a liability). Debiting cash again would be incorrect as cash is already received.

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Oct/Nov 2021

109. Consider the following statements:
Statement I : Amortisation is the process of writing off the value of tangible fixed assets like

mention it as prescribing a mandatory format for all entities in the way a specific Act does.

Oct/Nov 2020

119. Match List-I (Account Type) with List-II (Example from ABC Ltd. Balance Sheet).

List-I

P. Non-current Asset

Q. Current Asset (Stock)

R. Owner's Equity

S. Long-term Liability

List-II

1. Capital
2. Long term liabilities
3. Fixed assets
4. Stocks

(A) P-3, Q-4, R-1, S-2

(B) P-4, Q-3, R-2, S-1

(C) P-3, Q-1, R-4, S-2

(D) P-2, Q-4, R-1, S-3

Ans :

(A) P-3, Q-4, R-1, S-2

P. Non-current Asset corresponds to Fixed assets (3). Q. Current Asset (Stock) corresponds to Stocks (4). R. Owner's Equity is represented by Capital (1). S. Long-term Liability corresponds to Long term liabilities (2). The matching correctly aligns the accounting classifications with the specific items from the illustrated balance sheet.

May/June 2022

120. A business has the following balances: Sales ₹2,00,000; Purchases ₹1,50,000; Opening Stock ₹20,000; Closing Stock ₹10,000; Direct Expenses ₹5,000. What is the Gross Profit?

(A) ₹35,000

(B) ₹45,000

(C) ₹30,000

(D) ₹40,000

Ans :

(A) ₹35,000

Gross Profit = Sales - Cost of Goods Sold (COGS). First, calculate COGS using the formula: COGS = Opening Stock + Purchases + Direct Expenses - Closing Stock . COGS = ₹20,000 + ₹1,50,000 + ₹5,000 - ₹10,000 = ₹1,65,000. Now, calculate Gross Profit = ₹2,00,000 (Sales) - ₹1,65,000 (COGS) = ₹35,000.

Oct/Nov 2023

121. Which of the following items from the ABC Ltd. illustration for 2021-22 does NOT represent a use of cash?

(A) Purchase of fixed assets ₹10,000

(B) Repayment of long term loans ₹5,000

(C) Expenses ₹20,000

(D) Increase in receivables ₹2,000

Ans :

(D) Increase in receivables ₹2,000

A use of cash is a cash outflow. Purchase of assets, repayment of loans, and payment of expenses are all uses of cash. An increase in receivables means that sales were made on credit, and cash has not yet been received for those sales. It represents a non-cash increase in assets, not a use of cash.

May/June 2016

122. What is the key difference between a Profit and Loss Account and a Balance Sheet?

(A) The P&L Account shows assets, while the Balance Sheet shows liabilities.

(B) The P&L Account covers a period of time, while the Balance Sheet is for a point in time.

(C) The P&L Account uses real accounts, while the Balance Sheet uses nominal accounts.

(D) The P&L Account is prepared before the Trial Balance, while the Balance Sheet is prepared after.

Ans :

(B) The P&L Account covers a period of time, while the Balance Sheet is for a point in time.

The Profit and Loss Account summarizes financial performance (revenues and expenses) over an entire accounting period (e.g., a year). In contrast, the Balance Sheet presents the financial position (assets, liabilities, equity) at a specific single point in time (e.g., as on March 31st), often described as a "snapshot".

Oct/Nov 2009

123. If a company fails to make an adjustment for prepaid expenses, what is the impact on its financial statements?

(A) Expenses are understated, and profits are overstated.

(B) Liabilities are overstated, and profits are understated.

(C) Assets are understated, expenses are overstated, and profits are understated.

(D) Both assets and profits are overstated.

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both sides of the balance sheet, maintaining the equality of assets and liabilities.

May/June 2008

114. From the P&L Account of ABC for the year ended 31-3-2022, what is the total of the credit side?
(A) ₹2,00,000
(B) ₹1,99,000
(C) ₹1,70,000
(D) ₹2,10,000

Ans :

(D) ₹2,10,000
The credit side of a Profit and Loss account (or a combined Trading and P&L) records all incomes and gains. In the given example, the credit side consists of "By Sales" with an amount of ₹2,00,000 and "By closing stocks" with an amount of ₹10,000. The total of the credit side is ₹2,00,000 + ₹10,000 = ₹2,10,000.

Oct/Nov 2013

115. In the Cash Account of ABC Ltd., a payment of ₹1,70,000 is shown. What was this payment for?
(A) Payment for purchases
(B) Purchase of fixed assets
(C) Repayment of long-term liabilities
(D) Payment for expenses

Ans :

(A) Payment for purchases
By examining the credit (payment) side of the Cash Account provided in the illustration for ABC Ltd., the entry for ₹1,70,000 is listed against the particular "By purchase". This corresponds to the amount of purchases made during the year as shown in the Profit and Loss account, indicating payment made for those goods.

May/June 2015

116. What is the primary reason that the 'Stock Account' in the ledger does not reflect the correct value of stock on hand during the year?
(A) Because stock is valued only at the end of the year.
(B) Because entries for sales and purchases do not affect the stock account directly.
(C) Because stock is an intangible asset whose value is difficult to track.
(D) Because of continuous depreciation of stock value.

Ans :

(B) Because entries for sales and purchases do not affect the stock account directly.
In the system described, when goods are purchased, the 'Purchase Account' is debited, and when goods are sold, the 'Sales Account' is credited. The 'Stock Account' itself is not updated with each transaction. It only carries the opening balance until a physical count and valuation of closing stock is performed at year-end.

Oct/Nov 2012

117. If a company's financial statements are prepared without making an adjustment entry for accrued income, what will be the effect?
(A) Both assets and profits will be overstated.
(B) Assets will be understated, but profits will be overstated.
(C) Profits will be understated, but assets will be overstated.
(D) Both assets and profits will be understated.

Ans :

(D) Both assets and profits will be understated.
Accrued income is income that has been earned but not yet received. If it is not accounted for, the total income for the period will be understated, leading to an understatement of profit. Furthermore, the corresponding asset (income receivable) will not be recorded, leading to an understatement of total assets on the balance sheet.

May/June 2011

118. Which of the following formats for financial statements is NOT mentioned as being prescribed by a specific Act for certain entities in India?
(A) Format prescribed by the Generally Accepted Accounting Principles (GAAP) for all entities.
(B) Format prescribed by the Companies Act 2013 for companies.
(C) Format prescribed by the Banking Regulation Act for banks.
(D) Format prescribed by other Acts for specific types of companies.

Ans :

(A) Format prescribed by the Generally Accepted Accounting Principles (GAAP) for all entities.
The text specifies that formats are prescribed by the Companies Act 2013 and the Banking Regulation Act. It states that for "other business entities, there is no prescribed format." While GAAP provides principles, the text does not

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profit/loss), form the balance sheet. This implies that nominal accounts (income and expenditure) do not appear on the balance sheet directly. Their net effect is channeled through the P&L account into the equity section of the balance sheet.

May/June 2023

82. "Profit and Loss account shows only the net profit or net loss from operation of business while the Profit and Loss appropriation accounts shows all non-operational adjustments."
Which of the following items would be found in the P&L Appropriation account but NOT in the P&L account?
(A) Salary paid to employees.
(B) Proposed dividend for shareholders.
(C) Rent received from sub-letting a property.
(D) Cost of raw materials consumed.

Ans :

(B) Proposed dividend for shareholders.
The source distinguishes between operational items (P&L account) and non-operational adjustments/appropriations (P&L Appropriation account). Salary and cost of materials are operational expenses, and rent received is operational income. A proposed dividend is a distribution of profit after it has been earned, making it an appropriation, not an operational item.

Oct/Nov 2018

83. "Ind AS-1 states as to what constitutes a complete set of financial statements. The Profit and Loss Appropriation Account is not part of this set. Instead, the Standard prescribes a 'Statement of changes in equity'."
According to this information, for a company complying with Ind AS, which statement should be prepared to show profit appropriations?
(A) The Profit and Loss Appropriation Account.
(B) A separate Reserves and Surplus schedule.
(C) The Statement of changes in equity.
(D) The Director's Report.

Ans :

(C) The Statement of changes in equity.
The text explicitly states that under Ind AS-1, the Profit and Loss Appropriation Account is not considered part of a complete set of financial statements. It is replaced by the "Statement of changes in equity". This statement serves the purpose of showing profit appropriations and other equity-related changes in a more detailed manner.

May/June 2007

84. "For accounting purposes, a business entity is separate from its promoters (owners). The money invested by the promoters in this entity is called the capital (or risk capital)."
This description refers to which fundamental accounting concept?
(A) Going Concern Concept
(B) Accrual Concept
(C) Business Entity Concept
(D) Matching Concept

Ans :

(C) Business Entity Concept
The source describes the core idea of the Business Entity Concept, which treats the business as a distinct entity, separate from its owners. This is why the owner's investment (capital) is treated as a liability of the business to the owner, and the business's transactions are recorded independently from the owner's personal transactions.

Oct/Nov 2025

85. "Please note that the balance sheet is like a photograph of financial position (asset and liabilities) taken at a specific moment."
What does this analogy of a "photograph" imply about the balance sheet?
(A) It is a static report valid for a single point in time.
(B) It shows the financial performance over a long period.
(C) It is visually appealing and easy to understand for all stakeholders.
(D) It captures all future financial transactions of the company.

Ans :

(A) It is a static report valid for a single point in time.
The "photograph" analogy highlights the time-specific nature of the balance sheet. Just as a photo captures a scene at a precise instant, the balance sheet presents the company's assets, liabilities, and equity on a specific date. The very next moment, a new transaction could change this financial position, requiring a new "photograph".

NODIA

Ans :

(C) Assets are understated, expenses are overstated, and profits are understated.
If prepaid expenses are not adjusted, the entire amount paid is treated as an expense for the current period, overstating the expenses and understating the profit. Since the prepaid portion is not recognized as an asset ('Prepaid Expense'), the company's assets are also understated on the balance sheet.

May/June 2023

124. The final balance sheet of ABC Ltd. as on 31-3-2022 has total assets of ₹84,000. This total is composed of Fixed assets, Cash, Stocks, and Receivables. What are their respective values?
(A) ₹50,000, ₹15,000, ₹9,000, ₹6,000
(B) ₹60,000, ₹15,000, ₹10,000, ₹(-1,000)
(C) ₹50,000, ₹6,000, ₹9,000, ₹8,000
(D) ₹60,000, ₹6,000, ₹10,000, ₹8,000

Ans :

(D) ₹60,000, ₹6,000, ₹10,000, ₹8,000
Based on the chapter's final illustration, the values are calculated as: Fixed Assets = ₹50,000 (opening) + ₹10,000 (purchase) = ₹60,000. Cash = ₹6,000 (from cash account). Stocks = ₹10,000 (closing stock). Receivables = ₹6,000 (opening) + ₹2,000 (increase) = ₹8,000. The sum of these values is ₹84,000.

Oct/Nov 2018

125. Consider the following four items:
1. Provision for bad and doubtful debts
2. Writing off preliminary expenses
3. Provision for contingent events
4. Calculation of depreciation

Which of these are mentioned as "Other adjustments" in section 13.4.3?
(A) 1, 2 and 4
(B) 1, 3 and 4
(C) 1, 2 and 3
(D) 2, 3 and 4

Ans :

(C) 1, 2 and 3
Section 13.4.3, "Entries Relating to Other Items," explicitly lists "provision for bad and doubtful debts, writing off part of fictitious assets like preliminary expanses etc., provisioning for contingent events etc." as other adjustments. Depreciation is discussed separately and extensively in its own section (13.4.1) and is not listed here.

May/June 2007

126. Which of the following statements is/are incorrect regarding the preparation of financial statements?
1. Final accounts are prepared to show the financial position at the beginning of the accounting period.
2. An unadjusted trial balance is considered a complete financial statement.
3. Adjustment entries convert a company's accounting records from cash basis to accrual basis.

(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(A) 1 and 2 only
Statement 1 is incorrect; final accounts show the position at the end of the period. Statement 2 is incorrect; a trial balance is an internal worksheet, not a financial statement. Statement 3 is correct; this is the primary purpose of adjusting entries as they account for revenues and expenses when incurred, not when cash moves.

May/June 2016

127. **Assertion (A) :** On a balance sheet, the total of assets always equals the total of liabilities.
Reason (R) : Every business transaction has a dual aspect that affects two accounts, ensuring that for every debit there is an equal credit, which keeps the accounting equation in balance.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) states the fundamental principle of the balance sheet (Assets = Liabilities + Equity). Reason (R) correctly identifies the underlying mechanism, which is the double-entry system of accounting. Every transaction's dual effect

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For a company limited by shares, the liability of its members is limited by its memorandum to the nominal value of the shares they hold. If a member has already paid the full price of the shares, their liability is zero. If the shares are partly paid, their liability extends only to the unpaid amount.

Oct/Nov 2015

25. For what purpose are 'companies limited by guarantee' generally formed?

(A) For undertakings that require large amounts of initial share capital.
(B) For high-risk, high-profit business ventures.
(C) For the promotion of non-profit activities like sports, education, or art.
(D) For banking and financial service institutions.

Ans :

(C) For the promotion of non-profit activities like sports, education, or art.
Companies limited by guarantee are typically non-profit making organisations. Members guarantee to contribute a certain amount in the event of the company's winding up. This structure is suitable for promoting activities like sports, education, religion, and fine arts, where the primary objective is not commercial profit but promotion of a cause.

May/June 2020

26. Which of the following statements about a company with unlimited liability is correct?

(A) The liability of its members is unlimited, similar to partners in a firm.
(B) It cannot be incorporated under the Companies Act, 2013.
(C) It must have a minimum share capital of ₹1 crore.
(D) It can only be formed for charitable purposes.

Ans :

(A) The liability of its members is unlimited, similar to partners in a firm.
A company with unlimited liability is one where there is no limit on the liability of its members. In the event of winding up, if company assets are insufficient to pay its debts, the members are personally liable to contribute to its assets without any limitation, much like partners in a partnership firm.

NODIA

Oct/Nov 2021

27. Identify the incorrect statement regarding the distinction between a partnership and a limited company.

(A) Registration is compulsory for a company but not for a partnership.
(B) A partnership has perpetual existence, while a company does not.
(C) The liability of shareholders is limited, whereas the liability of partners is unlimited.
(D) The formation of a company involves more legal formalities than a partnership.

Ans :

(B) A partnership has perpetual existence, while a company does not.
This statement is incorrect as the opposite is true. A limited company enjoys perpetual existence, meaning its life is independent of its members. A partnership, however, does not have perpetual existence and can be dissolved upon the death, retirement, or insolvency of a partner, depending on the partnership agreement.

May/June 2013

28. What is the maximum number of members allowed in a partnership firm carrying on a banking business?

(A) Ten
(B) Two
(C) Twenty
(D) Two hundred

Ans :

(A) Ten
The rules for membership in a partnership firm vary by the nature of the business. For a partnership firm engaged in banking activities, the maximum number of partners is restricted to ten. For other types of business, the maximum number of partners allowed is typically twenty, which is different from company membership rules.

Oct/Nov 2008

29. How does ownership and management differ between a partnership and a company?

(A) In both, ownership and management are separated.
(B) In a company, ownership and management are combined; in a partnership, they are separate.
(C) In a partnership, ownership and management

CHAPTER 14

Company Accounts - I

Oct/Nov 2018

1. In the context of business expansion where capital requirements are large, which form of business organisation is most suitable?
(A) Proprietary firm
(B) Joint stock company
(C) Partnership firm
(D) Limited Liability Partnership

Ans :

(B) Joint stock company
While proprietary and partnership firms are suitable for small to medium capital needs, they are not ideal for large investments like setting up a cement factory. The joint stock company structure is designed to pool large amounts of capital from the public, making it the most suitable form for large-scale business organisations.

May/June 2005

2. What is the primary disadvantage of a partnership firm concerning the liability of its partners?
(A) Liability is unlimited, and personal assets of partners can be used to pay the firm's debts.
(B) Liability is limited to the capital contributed by each partner, with no recourse to personal property.
(C) Liability is determined by the Partnership Act, 1932, and is capped at a specific financial limit for all partners.
(D) Only the managing partner has unlimited liability, while all non-managing partners have liability limited to their investment.

Ans :

(A) Liability is unlimited, and personal assets of partners can be used to pay the firm's debts.
In a partnership firm, the liability of each partner is unlimited. This means if the firm's assets are insufficient to discharge its liabilities upon dissolution, the private property of individual partners can be legally used to settle the firm's debts. This is a significant risk compared to a limited liability structure.

Oct/Nov 2025

3. According to Section 2(20) of the Companies Act, 2013, what is the definition of a 'company'?
(A) A company is an association of persons who contribute money for a common purpose.
(B) A company is an artificial person created by law with perpetual succession.
(C) A company is a company incorporated under the Companies Act, 2013, or any previous company law.
(D) A company is a legal entity separate from its members, with a common seal.

Ans :

(C) A company is a company incorporated under the Companies Act, 2013, or any previous company law.
Section 2(20) of the Companies Act, 2013, provides a concise legal definition of a company. It defines a company as one that has been incorporated under the current Act (2013) or under any company law that existed prior to it. This definition emphasizes the legal process of incorporation as the basis of a company's existence.

May/June 2017

4. Which of the following is a mandatory requirement for a joint stock company under the Companies Act, 2013?
(A) Issuing shares to the public
(B) Having a minimum of 100 members
(C) Appointing a government director
(D) Compulsory registration

Ans :

(D) Compulsory registration
According to the Companies Act, 2013, it is compulsory to register a joint stock company. This process of registration, or incorporation, is what brings the company into existence as a legal entity. Unlike a partnership firm where registration is not compulsory, a company cannot exist legally without being registered under the Act.

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preference capital does not become a permanent part of the company's capital structure.

May/June 2008

34. Under what specific circumstance can a company issue preference shares for a period exceeding 20 years but not exceeding 30 years?
(A) If the company is a non-profit organisation.
(B) If the shares are issued to foreign institutional investors.
(C) If the company has not made a profit for three consecutive years.
(D) If the shares are issued for infrastructure projects.

Ans :

(D) If the shares are issued for infrastructure projects.
An exception to the 20-year redemption rule for preference shares is provided for companies engaged in infrastructure projects. These companies are permitted to issue preference shares for a term longer than twenty years, but not exceeding thirty years, subject to certain conditions regarding redemption from the twenty-first year onwards.

Oct/Nov 2012

35. What right do 'participating preference shares' grant to their holders?
(A) The right to participate in the surplus assets during winding up after equity capital is repaid.
(B) The right to participate in the day-to-day management of the company.
(C) The right to participate in surplus profits remaining after paying equity shareholders.
(D) The right to participate in the election of the Board of Directors.

Ans :

(A) The right to participate in the surplus assets during winding up after equity capital is repaid.
Participating preference shares carry an additional right beyond the standard fixed dividend and capital repayment. These shares have a right to participate in the surplus assets that remain in case of a winding-up, after the capital has been repaid to both preference and equity shareholders, unless stated otherwise.

May/June 2015

36. The capital stated in the 'Memorandum of Association' of a company, which is the maximum amount the company is authorised to raise, is known as:
(A) Issued Capital
(B) Authorised Capital
(C) Subscribed Capital
(D) Called-up Capital

Ans :

(B) Authorised Capital
Authorised Capital, also known as Nominal or Registered Capital, is the maximum amount of share capital that a company is permitted to issue to shareholders, as specified in its Memorandum of Association. This amount represents the upper limit of capital the company can raise and can only be increased by following legal procedures.

NODIA

Oct/Nov 2011

37. What is 'Issued Capital'?
(A) The part of authorised capital that the company offers to the public for subscription.
(B) The total amount of capital actually paid by shareholders.
(C) The total nominal value of shares for which applications have been received from the public.
(D) The amount of capital that the company has demanded from its shareholders.

Ans :

(A) The part of authorised capital that the company offers to the public for subscription.
Issued capital is that portion of the authorised capital which the company offers to investors for subscription. This may include shares issued to the public or to vendors for consideration other than cash. The amount of issued capital can be equal to or less than the authorised capital, but it can never exceed it.

May/June 2022

38. Which of the following best defines 'Subscribed Capital'?
(A) The maximum capital a company can issue.
(B) The portion of issued capital that has been actually subscribed by the public.
(C) The total amount of money called up by the company.
(D) The amount of capital paid by the shareholders.

May/June 2023

10. What is the rule regarding the transferability of shares in a public limited company?
(A) Shares are freely transferable without any restrictions.
(B) Shares can only be transferred with the approval of the Board of Directors.
(C) Shares can only be transferred to existing members of the company.
(D) Transfer of shares is prohibited by the Companies Act, 2013.

Ans :

(A) Shares are freely transferable without any restrictions.
The shares of a public company are freely transferable. This allows shareholders to sell their shares in the open market, providing liquidity for their investment. This is a significant distinction from a private limited company, where the right to transfer shares is typically restricted by the company's articles of association.

Oct/Nov 2022

11. Which statement correctly describes the membership requirements for a private limited company?
(A) Minimum 7 members and no maximum limit.
(B) Minimum 2 members and maximum 100 members.
(C) Minimum 1 member and maximum 50 members.
(D) Minimum 2 members and maximum 200 members.

Ans :

(D) Minimum 2 members and maximum 200 members.
A private limited company must have a minimum of two members to be formed. The Companies Act, 2013, sets the maximum number of members for a private company at two hundred. This limit on membership is one of the defining characteristics that distinguishes it from a public limited company, which has no upper limit.

May/June 2009

12. What are the membership limits for a public limited company?
(A) Minimum 2 members, maximum 200 members.
(B) Minimum 7 members, no maximum limit.
(C) Minimum 7 members, maximum 500 members.
(D) Minimum 50 members, no maximum limit.

Ans :

(B) Minimum 7 members, no maximum limit.
A public limited company requires a minimum of seven members for its formation. Unlike a private company, there is no maximum limit on the number of members it can have. This allows a public company to raise capital from a large number of investors through a public issue of shares.

Oct/Nov 2011

13. What change did the Companies (Amendment) Act, 2015, bring regarding the minimum paid-up capital requirement?
(A) It increased the minimum capital for private companies to ₹5 lakhs.
(B) It introduced a uniform minimum capital of ₹10 lakhs for all companies.
(C) It removed the requirement of minimum paid-up capital for both private and public companies.
(D) It made the minimum paid-up capital requirement applicable only to listed companies.

Ans :

(C) It removed the requirement of minimum paid-up capital for both private and public companies.
The Companies Act, 2013 initially prescribed a minimum paid-up capital of ₹1 lakh for a private company and ₹5 lakhs for a public company. However, the Companies (Amendment) Act, 2015, eliminated this requirement. Now, a company can be incorporated without any minimum paid-up capital, and the amount is left to its discretion.

May/June 2016

14. Match the type of company in List-I with its basis of classification in List-II.
List-I
P. Statutory Company
Q. Public Company
R. Company Limited by Shares
S. Subsidiary Company
List-II
1. Based on Liability
2. Based on Incorporation

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maintains this equality, making the reason a perfect explanation for the assertion.

Oct/Nov 2009

128. Which of the following statements concerning final accounts is correct?

(A) The Profit and Loss Appropriation Account is a part of the complete set of financial statements under Ind AS-1.

(B) The net profit or loss from the P&L account is eventually taken to the Balance Sheet.

(C) The closing stock figure is obtained directly from the trial balance.

(D) LIFO is the preferred method of inventory valuation as per Ind AS 2.

Ans :

(B) The net profit or loss from the P&L account is eventually taken to the Balance Sheet.

The net result from the P&L account (profit or loss) represents the change in owner's equity during the period. This amount is transferred to the capital or retained earnings account, which is a component of the liabilities and equity side of the Balance Sheet, thus ensuring the balance sheet reflects the period's performance.

May/June 2023

129. Consider the following statements regarding the flow of accounting information:

1. Balances from ledger accounts are used to prepare a trial balance.
2. The trial balance is adjusted for items like outstanding expenses and accrued income.
3. The adjusted trial balance is used to prepare the P&L Account and Balance Sheet.
4. Nominal accounts are closed by transferring them to the P&L account.

Which of the statements are correct?

(A) 1, 2 and 3 only

(B) 2, 3 and 4 only

(C) 1, 3 and 4 only

(D) All 1, 2, 3 and 4 are correct.

Ans :

(D) All 1, 2, 3 and 4 are correct.

All four statements accurately describe the standard process of preparing final accounts. It starts with the trial balance from ledgers (1), which is then adjusted (2). The final P&L and Balance Sheet are prepared from these adjusted balances (3). This involves closing all nominal accounts to the P&L account (4).

Oct/Nov 2018

130. Which of the following is the most appropriate description of a Trading Account?

(A) A part of the P&L account that calculates gross profit by matching sales with the cost of goods sold.

(B) A statement that lists all assets and liabilities of a trading concern.

(C) An account that records all cash transactions related to buying and selling goods.

(D) A summary of all indirect expenses incurred by the business during the year.

Ans :

(A) A part of the P&L account that calculates gross profit by matching sales with the cost of goods sold.

The most accurate description is that the Trading Account is a subsection of the overall income statement (P&L Account). Its specific function is to isolate direct revenues (sales) and direct costs (cost of goods sold) to compute the initial or 'gross' profit before considering any of the company's other operating, administrative, or financial expenses.

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Ans :

(C) A company which is not a private company.
Section 2(71) of the Companies Act, 2013, defines a public company by exclusion. It simply states that a public company is a company that is not a private company. This implies that it does not have the restrictions on membership numbers, share transferability, and public subscription that are characteristic of a private company.

May/June 2019

20. For a company to be classified as a Government Company, what is the minimum percentage of paid-up share capital that must be held by the government?
(A) 100%
(B) 75%
(C) More than 25%
(D) Not less than 51%

Ans :

(D) Not less than 51%
A company is designated as a Government Company if a minimum of 51% of its paid-up share capital is held by the Central Government, any State Government(s), or partly by the Central and partly by one or more State Governments. This controlling stake is the defining criterion for its classification as a government company.

Oct/Nov 2014

21. What is the relationship between a holding company and a subsidiary company?
(A) A holding company is one in which another company has significant influence.
(B) A holding company and a subsidiary company are equal partners in a joint venture.
(C) A holding company is one that controls the composition of the Board of Directors of another company.
(D) A holding company is a government-owned entity that regulates subsidiary companies.

Ans :

(C) A holding company is one that controls the composition of the Board of Directors of another company.
As per Section 2(46) and 2(87) of the Companies Act 2013, a holding company is one which has one or more subsidiary companies. A company is deemed a subsidiary if the holding company controls the composition of its Board of Directors or holds more than one-half of its total share capital.

May/June 2025

22. Which type of company is defined as having only one person as a member?
(A) One Person Company
(B) Private Company
(C) Associate Company
(D) Subsidiary Company

Ans :

(A) One Person Company
A One Person Company (OPC) is a specific type of company that, as its name suggests, is incorporated with only one person as its member. This structure was introduced by the Companies Act, 2013, to encourage individual entrepreneurs to operate within a corporate framework with the benefit of limited liability.

NODIA

Oct/Nov 2005

23. A company is considered a subsidiary of a holding company if the holding company controls more than what portion of its total share capital?
(A) One-fourth
(B) One-third
(C) One-half
(D) Two-thirds

Ans :

(C) One-half
According to Section 2(87) of the Companies Act, 2013, one of the conditions for a company to be a subsidiary is that the holding company exercises or controls more than one-half of the total share capital. This control can be exercised either on its own or together with one or more of its other subsidiary companies.

May/June 2010

24. In a 'company limited by shares', what is the extent of a member's liability?
(A) The guaranteed amount specified in the memorandum.
(B) The amount, if any, unpaid on the shares held by the member.
(C) The member's entire personal wealth.
(D) A proportion of the company's total liabilities.

Ans :

(B) The amount, if any, unpaid on the shares held by the member.

Oct/Nov 2012

5. Which feature of a company signifies that it is a legal entity distinct from its members?
(A) Perpetual succession
(B) Limited liability
(C) Artificial person
(D) Incorporated association

Ans :

(C) Artificial person
A company is considered an artificial person created by law. This legal status makes it a separate entity from its members. Consequently, it can own property, enter into contracts, sue, and be sued in its own name. Even a member can enter into a contract with the company, highlighting this distinct legal personality.

May/June 2021

6. What does the feature of 'perpetual succession' imply for a company?
(A) The company's management is passed down through hereditary lines.
(B) The company's existence is unaffected by the death or insolvency of its shareholders.
(C) The company must be re-registered every 20 years to continue its existence.
(D) The company can only be dissolved by a unanimous vote of all its shareholders.

Ans :

(B) The company's existence is unaffected by the death or insolvency of its shareholders.
Perpetual succession means that the company has a continuous existence. Its life is not dependent on the life of its members. The death, insolvency, or transfer of shares by any shareholder does not affect the company's existence. The company continues to exist until it is legally wound up according to the provisions of the Companies Act.

Oct/Nov 2006

7. What is the status of the common seal for a company according to the Companies (Amendment) Act, 2015?
(A) It is mandatory for all contracts and share certificates.
(B) It must be affixed and countersigned by a government official.
(C) It has been replaced by a digital signature for all purposes.
(D) Its use has been made optional.

Ans :

(D) Its use has been made optional.
While the Companies Act, 2013 required a common seal on certain documents, the Companies (Amendment) Act, 2015 made its use optional. Documents that previously required a common seal, like share certificates, can now instead be signed by two directors or by one director and the company secretary, if one is appointed.

May/June 2014

8. The liability of members in a joint stock company is typically limited to what extent?
(A) The face value of the shares held by them
(B) The total debts of the company
(C) An amount decided by the Board of Directors annually
(D) A percentage of the company's annual profit

Ans :

(A) The face value of the shares held by them
A key feature of a joint stock company is limited liability. This means a shareholder's liability is restricted to the amount, if any, remaining unpaid on the shares they hold. Their personal assets are protected and cannot be used to pay off the company's debts, unlike in a sole proprietorship or partnership firm.

Oct/Nov 2010

9. Who is responsible for the management of a company?
(A) The shareholders who are the true owners
(B) The government-appointed administrators
(C) The Board of Directors, elected by the shareholders
(D) The largest institutional investors

Ans :

(C) The Board of Directors, elected by the shareholders
A company exhibits a separation of management from ownership. While the shareholders are the owners, they do not participate directly in day-to-day management. Instead, they elect their representatives, known as the Board of Directors, to manage the company's affairs on their behalf, making strategic and operational decisions for the business.

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are combined; in a company, they are separate.
(D) In both, partners and shareholders directly manage the business.

Ans :

(C) In a partnership, ownership and management are combined; in a company, they are separate.
In a partnership, the partners are both the owners and the managers of the firm. In contrast, a company features a separation of ownership and management. The shareholders are the owners, but they delegate the management responsibility to an elected Board of Directors, who handle the day-to-day operations of the company.

May/June 2024

30. What are the two kinds of share capital a company limited by shares can have?
(A) Equity share capital and preference share capital
(B) Equity share capital and debenture capital
(C) Voting share capital and non-voting share capital
(D) Authorised share capital and issued share capital

Ans :

(A) Equity share capital and preference share capital
The share capital of a company limited by shares is primarily divided into two categories: equity share capital and preference share capital. Equity shares represent ownership with voting rights, while preference shares carry certain preferential rights regarding dividend payment and capital repayment, but usually have limited or no voting rights.

Oct/Nov 2017

31. What are the preferential rights enjoyed by preference shareholders?
(A) The right to vote on all company resolutions and receive bonus shares.
(B) The right to a higher dividend than equity shareholders and priority in management decisions.
(C) The right to appoint the company's auditors and approve the annual budget.
(D) The right to payment of a fixed rate dividend and return of capital on winding up, before equity shareholders.

Ans :

(D) The right to payment of a fixed rate dividend and return of capital on winding up, before equity shareholders.
Preference shares are defined by two key preferential rights. First, they have the right to receive dividends at a fixed rate before any dividend is paid to equity shareholders. Second, in the event of the company's winding up, they have the right to the return of their capital before the equity shareholders receive anything.

NODIA

May/June 2006

32. What is the defining characteristic of cumulative preference shares?
(A) Shareholders can convert them into equity shares at any time.
(B) The dividend rate increases every year.
(C) They grant the holder the right to participate in surplus profits.
(D) Unpaid dividends accumulate and are carried forward to future years.

Ans :

(D) Unpaid dividends accumulate and are carried forward to future years.
If a company does not make enough profit to pay the dividend on cumulative preference shares in a particular year, the unpaid dividend is not lost. It accumulates and is carried forward. In subsequent years with sufficient profits, the company must first pay all arrears of preference dividend before paying any dividend to equity shareholders.

Oct/Nov 2013

33. According to Section 55 of the Companies Act, 2013, what is the maximum period within which preference shares must generally be redeemed?
(A) 10 years from the date of issue
(B) 30 years from the date of issue
(C) 20 years from the date of issue
(D) 50 years from the date of issue

Ans :

(C) 20 years from the date of issue
Section 55 of the Companies Act, 2013, prohibits the issue of irredeemable preference shares. It mandates that preference shares must be redeemed within a period not exceeding twenty years from their date of issue. This ensures that

3. Based on Ownership
4. Based on Ownership

(A) P-2, Q-3, R-1, S-4
(B) P-1, Q-2, R-3, S-4
(C) P-2, Q-4, R-1, S-3
(D) P-3, Q-1, R-4, S-2

Ans :

(A) P-2, Q-3, R-1, S-4
Companies are classified on different bases. A Statutory Company is based on its mode of Incorporation (by a special Act). Public and Subsidiary Companies are classified based on their Ownership structure. A Company Limited by Shares is classified based on the Liability of its members. The correct matching reflects these distinct classification criteria.

Oct/Nov 2009

15. A company established under a special charter issued by a King or Head of State is known as a:
(A) Chartered company
(B) Statutory company
(C) Registered company
(D) Government company

Ans :

(A) Chartered company
A chartered company is one that is established under a special charter granted by a sovereign power, such as a King, Emperor, or Head of State. These types of companies, like the East India Company or the Bank of England, are not found in India and are primarily of historical significance in European countries.

May/June 2007

16. Life Insurance Corporation of India (LIC) and Air India are examples of which type of company?
(A) Chartered company
(B) Statutory company
(C) Registered company
(D) Holding company

Ans :

(B) Statutory company
A statutory company is created by a special Act passed by the Central or State Legislature. Organizations like the Life Insurance Corporation of India, Air India, and the Food Corporation of India were formed under specific Acts of Parliament. These companies are owned by the government and are granted independent legal status.

Oct/Nov 2019

17. A company incorporated in another country but having a place of business in India is called a:
(A) Subsidiary company
(B) Foreign company
(C) Associate company
(D) Transnational company

Ans :

(B) Foreign company
A foreign company is defined as a company that is incorporated outside India but establishes a place of business within India. An example would be the Hongkong and Shanghai Banking Corporation Ltd., which is incorporated outside India but operates branches and has a business presence within the country, making it a foreign company.

May/June 2012

18. Which of the following is NOT a condition for a company to be classified as a private company?
(A) It must have a minimum paid-up capital of ₹1 lakh.
(B) It limits the number of its members to two hundred.
(C) It prohibits any invitation to the public to subscribe for its securities.
(D) It restricts the right to transfer its shares.

Ans :

(A) It must have a minimum paid-up capital of ₹1 lakh.
A private company is defined by its articles, which must restrict share transferability, limit members to 200, and prohibit public subscription for securities. The requirement for a minimum paid-up capital of ₹1 lakh was removed by the Companies (Amendment) Act, 2015, and is therefore no longer a defining condition for a private company.

Oct/Nov 2024

19. According to Section 2(71) of the Companies Act, 2013, a public company is defined as:
(A) A company that is listed on a stock exchange.
(B) A company with more than 200 members.
(C) A company which is not a private company.
(D) A company in which the public holds at least 51% of the shares.

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Ans :

(B) The portion of issued capital that has been actually subscribed by the public.
Subscribed capital represents the nominal value of the shares from the issued capital that have been taken up or subscribed to by the public and other investors. It signifies the actual demand for the company's shares from a particular issue. This amount can be less than or, at most, equal to the issued capital.

Oct/Nov 2023

39. 'Called-up Capital' refers to:
(A) The total amount of capital paid by the shareholders.
(B) The portion of the subscribed capital that the company has asked shareholders to pay.
(C) The total nominal value of shares issued by the company.
(D) The maximum capital the company is authorised to raise.

Ans :

(B) The portion of the subscribed capital that the company has asked shareholders to pay.
Called-up capital is the part of the subscribed capital that the company has formally demanded or 'called' from its shareholders for payment. A company may decide to call the full nominal value of the shares at once or in instalments (e.g., application, allotment, calls). This amount represents the shareholders' current payment obligation.

May/June 2011

40. Which statement about 'Paid-up Capital' is correct?
(A) It can never be more than the called-up capital.
(B) It can be more than the called-up capital.
(C) It is the amount of capital stated in the Memorandum of Association.
(D) It is always equal to the issued capital.

Ans :

(A) It can never be more than the called-up capital.
Paid-up capital is the actual amount of money that shareholders have paid to the company against the called-up amount. Shareholders might default on calls, so the paid-up amount can be less than the called-up capital. However, shareholders cannot pay more than what has been called, so paid-up capital can never exceed the called-up capital.

Oct/Nov 2020

41. What is the term for a situation where the number of share applications received is greater than the number of shares offered by the company?
(A) Undersubscription
(B) Full subscription
(C) Oversubscription
(D) Minimum subscription

Ans :

(C) Oversubscription
Oversubscription occurs when a company receives applications for more shares than it has offered to the public through its prospectus. This typically happens when the company has good prospects and is well-regarded by investors. In such a scenario, the company cannot allot more shares than it offered and must use a basis of allotment.

May/June 2018

42. In a public issue, who is responsible for ensuring that the basis of allotment is finalised in a fair and proper manner?
(A) The regional stock exchange, lead merchant banker, and registrars to the issue.
(B) The company's Board of Directors, who hold ultimate responsibility for all shareholder-related matters.
(C) The Securities and Exchange Board of India (SEBI), which must provide direct approval for the allotment list.
(D) The company's independent auditors, who are required to review and certify the final allotment numbers.

Ans :

(A) The regional stock exchange, lead merchant banker, and registrars to the issue.
To ensure fairness in the allotment process, especially in cases of oversubscription, the responsibility is shared. The regional stock exchange, along with the post-issue lead merchant banker and the registrars to the issue, must ensure that the allotment is finalized according to the prescribed guidelines, such as proportionate allotment across categories.

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like the number of shares, current market price, and the class of employees or directors receiving them.

May/June 2025

62. What does an 'Employee Stock Option Scheme (ESOS)' grant to an employee?
(A) A right, but not an obligation, to apply for shares at a pre-determined price.
(B) An obligation to buy company shares at a future date.
(C) Fully paid bonus shares upon achieving performance targets.
(D) A monthly cash bonus equivalent to the value of one share.

Ans :

(A) A right, but not an obligation, to apply for shares at a pre-determined price.
An ESOS is a scheme that gives employees the option or right to purchase shares of the company at a price that is pre-determined at the time the option is granted. The employee is not obligated to exercise this right; they can choose to do so during a specified period if it is financially advantageous.

Oct/Nov 2005

63. What is the final step a company must take before it can pass a resolution to forfeit a shareholder's shares for non-payment of dues?
(A) Publish the shareholder's name in a national newspaper.
(B) Obtain a court order for the forfeiture.
(C) Send the shareholder a final notice giving them fourteen days to pay.
(D) Get approval from 75% of the other shareholders.

Ans :

(C) Send the shareholder a final notice giving them fourteen days to pay.
The process of forfeiture requires the company to first send reminders for payment. If the shareholder continues to default, the company must then send a final notice. This notice must state that if the dues are not paid within a period of fourteen days, the shares will be liable to be forfeited.

May/June 2010

64. What is the effect of forfeiture of shares?
(A) The name of the defaulting shareholder is cancelled from the register of members.
(B) The shareholder's liability is increased.
(C) The shares are automatically transferred to the company's CEO.
(D) The company has to refund the amount already paid by the shareholder.

Ans :

(A) The name of the defaulting shareholder is cancelled from the register of members.
Forfeiture of shares results in the cancellation of the membership of the defaulting shareholder. Their name is removed from the register of members, and they lose all rights associated with the shares. The amount they have already paid on these shares is forfeited to the company and is not refunded.

Oct/Nov 2015

65. When forfeiting shares, which account is debited with the amount called up per share on the forfeited shares?
(A) Forfeited Shares a/c
(B) Calls in Arrears a/c
(C) Share Capital a/c
(D) Share Premium a/c

Ans :

(C) Share Capital a/c
In the journal entry for forfeiture, the Share Capital account is debited. This is done to reverse the credit that was originally made to the Share Capital account when the shares were issued and called up. The amount of the debit is the called-up value per share multiplied by the number of shares being forfeited.

May/June 2020

66. If shares originally issued at a premium are forfeited, and the premium amount has not been received, what is the accounting treatment for the unpaid premium?
(A) The Share Premium account is debited.
(B) It is ignored in the forfeiture entry.
(C) It is credited to the Capital Reserve account.
(D) The Forfeited Shares account is debited.

Ans :

(A) The Share Premium account is debited.
When shares issued at a premium are forfeited, and the premium amount was due but not paid by the shareholder, the Share Premium account must be debited. This action reverses the credit

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(D) The amount is held in the Share Allotment account until the call is made.

Ans :

(A) The amount is credited to the relevant call account (e.g., First Call a/c).
As stated in the extract, when excess application money remains even after covering the allotment dues, the company may decide to adjust it against future calls. In this case, the amount is credited to the specific call accounts, such as the First Call account or Second Call account, effectively treating it as an advance payment for those calls.

May/June 2019

48. A company offered 1,000 shares of ₹100 each, with ₹50 payable on application. It received 2,100 applications. The board decided to accept 100 applications in full, reject 200 applications, and allot the remaining 900 shares on a pro-rata basis to the remaining 1,800 applicants. What is the amount of excess application money received from the pro-rata category?
(A) ₹90,000
(B) ₹10,000
(C) ₹50,000
(D) ₹45,000

Ans :

(D) ₹45,000
The pro-rata applicants applied for 1,800 shares but were allotted only 900 shares. The number of excess shares applied for in this category is 1,800 - 900 = 900 shares. Since the application money is ₹50 per share, the total excess application money received from this category is 900 × ₹50 = ₹45,000.

Oct/Nov 2018

49. In the context of the case from Question 48, what is the total amount of application money received by the company?
(A) ₹50,000
(B) ₹1,00,000
(C) ₹1,05,000
(D) ₹90,000

Ans :

(C) ₹1,05,000
The company received a total of 2,100 applications. The application money was specified as ₹50 per share. Therefore, the total application money received by the company is the total number of applications multiplied by the application money per share, which is 2,100 × ₹50 = ₹1,05,000.

May/June 2021

50. Based on the case from Question 48, what is the journal entry for the adjustment of application money?
(A) Dr. Share Applications a/c ₹1,05,000; Cr. Share Capital a/c ₹1,05,000
(B) Dr. Share Applications a/c ₹1,05,000; Cr. Share Capital a/c ₹50,000; Cr. Bank a/c ₹10,000; Cr. Share Allotment a/c ₹45,000
(C) Dr. Share Applications a/c ₹1,05,000; Cr. Share Capital a/c ₹50,000; Cr. Bank a/c ₹55,000
(D) Dr. Bank a/c ₹1,05,000; Cr. Share Applications a/c ₹1,05,000

Ans :

(B) Dr. Share Applications a/c ₹1,05,000; Cr. Share Capital a/c ₹50,000; Cr. Bank a/c ₹10,000; Cr. Share Allotment a/c ₹45,000
The total application money of ₹1,05,000 is adjusted as follows: ₹50,000 (1,000 shares × ₹50) is transferred to Share Capital; ₹10,000 (200 rejected shares × ₹50) is refunded via Bank; and the excess ₹45,000 from pro-rata applicants is transferred to the Share Allotment account to be adjusted against future dues.

Oct/Nov 2024

51. What is the maximum amount that can be demanded as a single call on a share?
(A) 25% of the face value of the share.
(B) 10% of the face value of the share.
(C) 50% of the face value of the share.
(D) The entire remaining amount after allotment.

Ans :

(A) 25% of the face value of the share.
There is a general stipulation that a single call amount should not exceed 25% of the nominal or face value of the share. If the balance due after allotment is more than 25% of the face value, the company must split the amount into two or more separate calls.

May/June 2017

52. If a first call of ₹5 is made on 1,000 shares, but payment is received for only 900 shares, what is the balance in the Share First Call account?
(A) ₹500 Debit
(B) ₹5,000 Credit

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Oct/Nov 2023

81. Continuing with Rahul Ltd. from Question 80, the company decides to use minimum free reserves for the ₹5,00,000 bonus issue. It uses Share Premium (₹1,00,000) and Capital Reserve (₹50,000). How much will be utilized from the General Reserve (available ₹3,00,000) and Profit & Loss Account (available ₹1,00,000)?

(A) ₹3,00,000 from General Reserve and ₹50,000 from P&L Account.
(B) ₹2,50,000 from General Reserve and ₹1,00,000 from P&L Account.
(C) ₹3,50,000 from General Reserve only.
(D) ₹1,75,000 from General Reserve and ₹1,75,000 from P&L Account.

Ans :

(A) ₹3,00,000 from General Reserve and ₹50,000 from P&L Account.
The total requirement is ₹5,00,000. After using Share Premium (₹1,00,000) and Capital Reserve (₹50,000), the shortfall is ₹3,50,000. To use minimum free reserves, the company will first exhaust the full General Reserve of ₹3,00,000. The remaining balance of ₹50,000 will then be taken from the Profit & Loss Account.

May/June 2018

82. After the bonus issue in the case of Rahul Ltd. from Question 80, what will be the new Issued and Paid-up Share Capital of the company?

(A) ₹5,00,000
(B) ₹12,50,000
(C) ₹10,00,000
(D) ₹15,00,000

Ans :

(C) ₹10,00,000
The initial Issued and Paid-up Capital was ₹5,00,000 (5,000 shares of ₹100). The company issued 5,000 new bonus shares of ₹100 each, valued at ₹5,00,000. The new total Issued and Paid-up Capital will be the sum of the old capital and the bonus issue, which is ₹5,00,000 + ₹5,00,000 = ₹10,00,000.

Oct/Nov 2016

83. A Ltd. Co. invited applications for 10,000 shares but received applications for only 9,000 shares. This situation is known as:

(A) Oversubscription
(B) Pro-rata allotment
(C) Undersubscription
(D) Forfeiture

Ans :

(C) Undersubscription
Undersubscription occurs when the number of shares applied for by the public is less than the number of shares offered by the company. In this case, the company offered 10,000 shares but only received applications for 9,000. All calculations for allotment and calls will therefore be based on the 9,000 shares subscribed.

May/June 2007

84. 200 shares were forfeited for non-payment of the second and final call of ₹20 per share. The shares were fully called up at ₹100. These shares were then re-issued as fully paid for ₹90 per share. What is the amount transferred to the Capital Reserve account?

(A) ₹18,000
(B) ₹16,000
(C) ₹14,000
(D) ₹2,000

Ans :

(C) ₹14,000
The amount paid on each forfeited share was ₹100 - ₹20 (unpaid call) = ₹80. For 200 shares, the total forfeited amount is 200 × ₹80 = ₹16,000. The discount on re-issue is ₹100 - ₹90 = ₹10 per share, totaling 200 × ₹10 = ₹2,000. The amount transferred to Capital Reserve is ₹16,000 (forfeited amount) - ₹2,000 (discount) = ₹14,000.

Oct/Nov 2007

85. What is the journal entry to record the forfeiture of the 200 shares in the case from Question 84?

(A) Dr. Equity Share Capital a/c ₹20,000; Cr. Calls in Arrear a/c ₹4,000; Cr. Forfeited Shares a/c ₹16,000.
(B) Dr. Equity Share Capital a/c ₹16,000; Cr. Calls in Arrear a/c ₹4,000; Cr. Forfeited Shares a/c ₹12,000.
(C) Dr. Forfeited Shares a/c ₹16,000; Cr. Equity Share Capital a/c ₹16,000.
(D) Dr. Equity Share Capital a/c ₹20,000; Cr. Bank a/c ₹16,000; Cr. Calls in Arrear a/c ₹4,000.

Ans :

(A) Dr. Equity Share Capital a/c ₹20,000; Cr. Calls in Arrear a/c ₹4,000; Cr. Forfeited Shares a/c ₹16,000.

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shown on the liabilities and equity side under the major head 'Shareholders' Funds' and the sub-head 'Reserves and Surplus'. It is a part of the company's accumulated reserves and is not part of the paid-up share capital.

May/June 2005

58. Read Section 53 of the Companies Act, 2013, as described below and answer the question.

"Except as provided in section 54 (issue of sweat equity), a company shall not issue shares at a discount. Any share issued by a company at a discounted price shall be void. Where any company fails to comply... such company and every officer... shall be liable to a penalty which may extend to an amount equal to the amount raised through the issue of shares at a discount or five lakh rupees, whichever is less..."

What is the consequence for a company that issues shares at a discount in violation of Section 53?

(A) The shares are void, and the company is liable for a penalty.
(B) The issue is valid, but the directors are imprisoned.
(C) The discount is treated as a loss in the Profit and Loss Account.
(D) The shareholders must pay the discount amount back to the company.

Ans :

(A) The shares are void, and the company is liable for a penalty.

Section 53 is explicit that any share issued at a discount (other than sweat equity) is void, meaning the issue is legally invalid. Furthermore, the company and its defaulting officers face a penalty. The penalty is the lesser of the amount raised via the discounted issue or five lakh rupees (₹5,00,000).

Oct/Nov 2019

59. Under what condition can a company legally issue shares at a discount?

(A) When issuing shares to the public for the first time.
(B) When the company is incurring continuous losses.
(C) When issuing 'Sweat Equity Shares' to employees or directors.
(D) When authorized by a resolution of the Board of Directors.

Ans :

(C) When issuing 'Sweat Equity Shares' to employees or directors.

The general prohibition on issuing shares at a discount under Section 53 of the Companies Act, 2013, has one specific exception. This exception is provided under Section 54, which permits the issue of 'Sweat Equity Shares' to directors or employees at a discount or for consideration other than cash.

May/June 2012

60. 'Sweat Equity Shares' can be issued for which of the following considerations?

(A) For providing know-how or making available rights in the nature of intellectual property.
(B) Only for cash at a discounted price.
(C) In exchange for physical assets contributed by an employee.
(D) As a reward for completing 20 years of service in the company.

Ans :

(A) For providing know-how or making available rights in the nature of intellectual property.

The definition of 'Sweat Equity Shares' under the Companies Act, 2013, specifies that they are issued to employees or directors. This can be at a discount or for a consideration other than cash, such as for providing valuable know-how, intellectual property rights, or other forms of value additions to the company.

Oct/Nov 2006

61. What is required for a company to issue sweat equity shares?

(A) An ordinary resolution passed by the board of directors.
(B) Approval from the Securities and Exchange Board of India (SEBI).
(C) A special resolution passed by the company in a general meeting.
(D) Consent from at least 75% of the employees.

Ans :

(C) A special resolution passed by the company in a general meeting.

As per Section 54 of the Companies Act 2013, one of the key conditions for issuing sweat equity shares is that the issue must be authorised by a special resolution passed by the company's shareholders. This resolution must specify details

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(C) ₹4,500 Debit
(D) ₹500 Credit

Ans :

(A) ₹500 Debit
The Share First Call account is debited with the total amount due, which is 1,000 × ₹5 = ₹5,000. It is then credited with the amount received, which is 900 × ₹5 = ₹4,500. The resulting balance in the account will be a debit of ₹5,000 - ₹4,500 = ₹500, representing the unpaid amount (calls in arrear).

Oct/Nov 2009

53. What is the purpose of opening a 'Calls in Arrear Account'?
(A) To consolidate all unpaid call amounts from various call accounts into a single account.
(B) It is a legally mandatory account to record all calls made by the company.
(C) To record payments received in advance for future calls.
(D) To set aside a provision for potential defaults on call payments.

Ans :

(A) To consolidate all unpaid call amounts from various call accounts into a single account.
While not legally required, companies may choose to open a 'Calls in Arrear Account'. Its purpose is to transfer the unpaid balances from individual call accounts (like First Call, Second Call) into one consolidated account. This provides a clear overview of the total amount of calls that are currently overdue from shareholders.

May/June 2016

54. What is the maximum rate of interest a company can pay on 'Calls in Advance' as per its Articles?
(A) 12% per annum
(B) 10% per annum
(C) 8% per annum
(D) 6% per annum

Ans :

(D) 6% per annum
If permitted by its Articles of Association, a company may accept payments for uncalled amounts in advance. On this amount, known as 'Calls in Advance', the company can pay interest. However, the interest rate paid cannot be more than 6% per annum for the period from receipt until the call becomes due.

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Oct/Nov 2010

55. Where is the 'Calls in Advance' account shown in the company's balance sheet?
(A) Under the head 'Reserves and Surplus'.
(B) As a deduction from 'Share Capital'.
(C) Separately between 'Share Capital' and 'Reserves and Surplus'.
(D) Under 'Current Liabilities'.

Ans :

(C) Separately between 'Share Capital' and 'Reserves and Surplus'.
The amount received as 'Calls in Advance' is not part of the company's paid-up capital until the call is officially made. Therefore, it is shown as a separate line item on the liabilities side of the balance sheet, typically positioned between the 'Share Capital' heading and the 'Reserves and Surplus' heading.

May/June 2023

56. Which of the following is NOT a permissible use of the amount collected as 'Share Premium'?
(A) Paying dividends to shareholders.
(B) Issuing fully paid bonus shares.
(C) Writing off preliminary expenses of the company.
(D) For the buy-back of the company's own shares.

Ans :

(A) Paying dividends to shareholders.
Share premium is a capital profit and is not available for distribution as dividends. The Companies Act specifies its use for limited purposes, which include issuing bonus shares, writing off certain expenses like preliminary expenses or commission on share issue, paying for premium on redemption of shares, and for the buy-back of shares.

Oct/Nov 2022

57. Under which head is the 'Share Premium' account recorded in the balance sheet?
(A) Share Capital
(B) Current Liabilities
(C) Non-current Liabilities
(D) Reserves and Surplus

Ans :

(D) Reserves and Surplus
The Share Premium account represents a capital profit for the company. In the balance sheet, it is

entry that was made when the premium became due, as the amount was never actually received by the company.

Oct/Nov 2021

67. A share of ₹100, fully called up, is forfeited for non-payment of a final call of ₹40. The company re-issues this share as fully paid-up for ₹80. What is the total amount received on this share that exceeds its face value?
(A) ₹60
(B) ₹20
(C) ₹40
(D) ₹80

Ans :

(C) ₹40
The old shareholder paid ₹100 - ₹40 = ₹60 before forfeiture. The new shareholder paid ₹80 upon re-issue. The total amount received by the company for this share is ₹60 + ₹80 = ₹140. Since the face value is ₹100, the excess amount is ₹140 - ₹100 = ₹40, which is transferred to the Capital Reserve.

May/June 2013

68. When forfeited shares are re-issued, any excess amount from the total received (amount forfeited + re-issue price) over the face value of the shares is transferred to which account?
(A) Capital Reserve Account
(B) General Reserve
(C) Profit and Loss Account
(D) Share Premium Account

Ans :

(A) Capital Reserve Account
The profit made on the re-issue of forfeited shares is a capital profit, not a revenue profit. Therefore, any surplus remaining after the re-issue—that is, the amount in the Forfeited Shares account less any discount on re-issue—is transferred to the Capital Reserve account. This amount is not available for dividend distribution.

Oct/Nov 2008

69. A share of ₹10, issued at a 10% discount, is forfeited for non-payment of the first and final call of ₹3. What is the amount credited to the Forfeited Shares account?
(A) ₹10
(B) ₹3
(C) ₹6
(D) ₹7

Ans :

(C) ₹6
The face value is ₹10 and the discount is ₹1 (10% of ₹10). The call in arrears is ₹3. The total amount paid by the shareholder is the face value minus the discount and the arrears. Therefore, the amount forfeited is ₹10 - ₹1 - ₹3 = ₹6. This is the amount credited to the Forfeited Shares account.

May/June 2024

70. 100 shares of ₹100 each were issued at a 5% discount. The second and final call of ₹20 has not been made. The shares are forfeited for non-payment of allotment (₹20) and first call (₹20). What is the called-up capital per share?
(A) ₹80
(B) ₹100
(C) ₹60
(D) ₹75

Ans :

(A) ₹80
The face value is ₹100. The second and final call of ₹20 has not been made. Therefore, the amount called up by the company per share at the time of forfeiture is the total face value minus the uncalled amount. This is calculated as ₹100 - ₹20 = ₹80.

Oct/Nov 2017

71. Madhav held 50 shares of ₹10 each, issued at a 10% premium. He did not pay the allotment money of ₹3 (including ₹1 premium) and the first call of ₹2. His shares were forfeited. What amount is debited to the Share Premium account upon forfeiture?
(A) ₹100
(B) ₹150
(C) ₹0
(D) ₹50

Ans :

(D) ₹50
Madhav failed to pay the allotment money, which included the premium. Since the premium of ₹1 per share was not received on his 50 shares, the Share Premium account must be debited to reverse the amount that was previously recorded as due. The total amount to be debited is 50 shares × ₹1/share = ₹50.

May/June 2006

72. What are bonus shares?

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Oct/Nov 2016

43. According to SEBI regulations, what is the prescribed range for the minimum application value in an initial public offer (IPO)?
(A) ₹10,000 to ₹15,000
(B) ₹5,000 to ₹10,000
(C) ₹15,000 to ₹20,000
(D) ₹1,000 to ₹5,000

Ans :

(A) ₹10,000 to ₹15,000
For an initial public offer of shares, SEBI guidelines stipulate that the minimum application size in terms of value should fall within the range of ₹10,000 to ₹15,000. This regulation aims to standardize the minimum investment size for retail investors applying for shares in an IPO, ensuring broader participation.

May/June 2007

44. What is the time limit within which the entire subscription money for a share issue should normally be called?
(A) Six months from the date of allotment.
(B) Twenty-four months from the date of allotment.
(C) Twelve months from the date of allotment.
(D) There is no specific time limit.

Ans :

(C) Twelve months from the date of allotment.
When subscription money is to be received in cash, the calls must be structured so that the entire amount is called up within twelve months from the date of allotment. This ensures that the company receives the full capital for the issued shares in a reasonable timeframe, providing certainty to both the company and the investors.

Oct/Nov 2007

45. What is the initial accounting entry passed when a company receives money for share applications?
(A) Debit Share Capital a/c, Credit Bank a/c
(B) Debit Share Applications a/c, Credit Share Capital a/c
(C) Debit Bank a/c, Credit Share Applications a/c
(D) Debit Bank a/c, Credit Share Allotment a/c

Ans :

(C) Debit Bank a/c, Credit Share Applications a/c
When application money is received, it does not yet constitute share capital as shares have not been allotted. Therefore, the money received is first recorded by debiting the Bank account and crediting a temporary account called the Share Applications account. This reflects the receipt of funds pending the allotment of shares.

May/June 2014

46. In a pro-rata allotment scenario, what is done with the excess application money received from applicants who are allotted shares?
(A) It is immediately forfeited by the company and treated as a capital profit.
(B) It is always refunded to the applicants in full, as per regulatory requirements.
(C) It is transferred to a general reserve account to be used for future corporate purposes.
(D) It is adjusted towards the amount due on share allotment and possibly future calls.

Ans :

(D) It is adjusted towards the amount due on share allotment and possibly future calls.
In a pro-rata allotment, applicants are allotted fewer shares than they applied for. The excess application money they paid is typically not refunded immediately. Instead, it is used to offset the amount they need to pay at the next stage, which is the share allotment. Any remaining excess may be adjusted against future calls.

Oct/Nov 2025

47. Read the following extract and answer the question below.
"If the excess amount received on applications is more than the full allotment dues, then the balance available after adjusting allotment dues may be either refunded or adjusted towards calls as per Board's decision taking into account the SEBI guidelines. If the excess is refunded, the bank account is suitably credited. If the same is adjusted towards future calls the same is credited to the First Call account and Second Call account as the case may be."
What is the correct accounting treatment if excess application money, after adjusting for allotment, is to be used for a future call?
(A) The amount is credited to the relevant call account (e.g., First Call a/c).
(B) The amount is credited to the Share Premium account.
(C) The amount is debited from the Bank account.

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holders.
(D) The bonus issue guidelines do not apply to companies with convertible debentures.

Ans :

(A) Reserve bonus shares for the debenture holders in proportion to the convertible part.
The guidelines aim to protect the interests of holders of convertible instruments. If a bonus issue is declared, the company must reserve shares for these holders. This ensures that when they convert their debentures into equity, they receive a similar benefit as the existing equity shareholders, maintaining fairness.

Oct/Nov 2012

77. When bonus shares are issued to make partly paid shares fully paid, which reserves cannot be used?
(A) General Reserve and Profit and Loss a/c
(B) Sinking Fund and General Reserve
(C) Capital Redemption Reserve and Share Premium accounts
(D) Debentures Redemption Reserve and Capital Reserve

Ans :

(C) Capital Redemption Reserve and Share Premium accounts
The accounting procedure specifies that for making partly paid shares into fully paid-up ones through a bonus, the provision must be created from various reserve accounts except the Capital Redemption Reserve and Share Premium accounts. These two reserves can only be used for issuing fully paid bonus shares, not for paying up calls.

May/June 2011

78. What is the journal entry to make the final call due on partly-paid shares before a bonus issue converts them to fully-paid?
(A) Dr. Equity Share Final Call a/c, Cr. Equity Share Capital a/c
(B) Dr. Bonus to Shareholders a/c, Cr. Equity Share Final Call a/c
(C) Dr. General Reserve a/c, Cr. Equity Share Capital a/c
(D) Dr. Equity Share Capital a/c, Cr. Equity Share Final Call a/c

Ans :

(A) Dr. Equity Share Final Call a/c, Cr. Equity Share Capital a/c
The first step in the process is to make the final call due. This is a standard call entry where the 'Equity Share Final Call account' is debited to create a receivable from shareholders, and the 'Equity Share Capital account' is credited to increase the nominal value of the capital called up.

Oct/Nov 2020

79. What is the final journal entry for the issue of fully paid bonus shares?
(A) Dr. General Reserve a/c, Cr. Equity Share Capital a/c
(B) Dr. Share Premium a/c, Cr. Bonus to Shareholders a/c
(C) Dr. Bonus to Shareholders a/c, Cr. Equity Share Capital a/c
(D) Dr. Bonus to Shareholders a/c, Cr. Bank a/c

Ans :

(C) Dr. Bonus to Shareholders a/c, Cr. Equity Share Capital a/c
After the necessary amount has been accumulated in the 'Bonus to Shareholders account' by debiting various reserves, the final step is the actual issue of shares. This is recorded by debiting the 'Bonus to Shareholders account' (to close it) and crediting the 'Equity Share Capital account' to reflect the increase in share capital.

May/June 2022

80. Rahul Ltd. has 5,000 equity shares of ₹100 each. The board decides to issue one bonus share for each share held. The company has Share Premium of ₹1,00,000 and Capital Reserve of ₹50,000. How much is the total value of the bonus issue?
(A) ₹1,50,000
(B) ₹10,00,000
(C) ₹5,00,000
(D) ₹4,50,000

Ans :

(C) ₹5,00,000
The company has 5,000 existing shares and is issuing one bonus share for each share held. This means 5,000 new bonus shares will be issued. The face value of each share is ₹100. Therefore, the total value of the bonus issue is 5,000 shares × ₹100/share = ₹5,00,000.

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(A) Shares issued to existing equity shareholders free of cost by capitalising reserves.
(B) Shares issued to the public at a discounted price, which is a common fundraising method.
(C) Shares offered to employees as part of an ESOS plan to promote employee ownership.
(D) Additional shares given to preference shareholders as a form of participating dividend.

Ans :

(A) Shares issued to existing equity shareholders free of cost by capitalising reserves.
Bonus shares are additional shares given to the current shareholders without any additional cost, based upon the number of shares that a shareholder owns. They are issued by converting the company's reserves and surplus (profits) into share capital, a process known as the capitalisation of reserves.

Oct/Nov 2013

73. As per Section 63 of the Companies Act 2013, a company may issue fully paid-up bonus shares to its members out of:
(a) its free reserves;
(b) the securities premium account; or
(c) the capital redemption reserve account.
Provided that no issue of bonus shares shall be made by capitalising reserves created by the revaluation of assets.
Which of the following reserves CANNOT be used for issuing bonus shares?
(A) General Reserve
(B) Securities Premium Account
(C) Revaluation Reserve
(D) Capital Redemption Reserve

Ans :

(C) Revaluation Reserve
Section 63 of the Companies Act, 2013, explicitly prohibits the capitalisation of reserves created by the revaluation of assets for the purpose of issuing bonus shares. While free reserves, securities premium, and capital redemption reserve are permissible sources, the unrealized profit from revaluing assets cannot be used.

May/June 2008

74. Which of the following is a pre-condition for a company to issue bonus shares under Section 63 of the Companies Act, 2013?
(A) The company must have paid dividends for the last three consecutive years.
(B) The company must be listed on a recognized stock exchange.
(C) The partly paid-up shares, if any, must be made fully paid-up.
(D) The company must obtain approval from the Central Government.

Ans :

(C) The partly paid-up shares, if any, must be made fully paid-up.
Section 63(2) lays down several conditions for a bonus issue. One crucial condition is that if the company has any partly paid-up shares outstanding on the date of allotment, they must first be made fully paid-up. A company cannot issue bonus shares while some of its existing shares are not fully paid.

Oct/Nov 2014

75. A company is generally free to decide the order of utilization of reserves for a bonus issue. However, which reserves are typically used first?
(A) Capital redemption reserve, share premium, and capital reserve.
(B) General reserve and profit and loss account.
(C) Sinking fund and debenture redemption reserve.
(D) Free reserves only.

Ans :

(A) Capital redemption reserve, share premium, and capital reserve.
While the company can decide the order, it is general practice to first utilize reserves that are not 'free' and have restricted uses. Capital Redemption Reserve, Share Premium, and Capital Reserve fall into this category as they cannot be used for dividend distribution but can be used for bonus issues.

May/June 2015

76. According to SEBI's 'Disclosure and Investor's Protection Guidelines' 2000, what must a company do if it announces a bonus issue while it has convertible debentures (FCDs/PCDs) pending conversion?
(A) Reserve bonus shares for the debenture holders in proportion to the convertible part.
(B) Postpone the bonus issue until all debentures are converted.
(C) Get special permission from the debenture

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The Share Capital account is debited with the called-up value (200 shares × ₹100 = ₹20,000). The Calls in Arrear account is credited with the unpaid amount (200 shares × ₹20 = ₹4,000). The Forfeited Shares account is credited with the amount already paid by the shareholder (200 shares × ₹80 = ₹16,000).

May/June 2014

86. Maharaja Ltd. issued 1,000 shares but received applications for 1,500 shares. Allotment was made on a pro-rata basis. What is the ratio of shares allotted to shares applied for?
(A) 2:3
(B) 1:2
(C) 3:4
(D) 1:1.5

Ans :

(A) 2:3
The company allotted 1,000 shares against 1,500 applications. The ratio of allotment is the number of shares allotted divided by the number of shares applied for, which is 1,000 : 1,500. Simplifying this ratio gives 2 : 3. This means for every 3 shares an applicant applied for, they were allotted 2 shares.

Oct/Nov 2025

87. In the case of Maharaja Ltd. from Question 86, Mr. Raja, who was allotted 30 shares, failed to pay the final call of ₹2. His shares were forfeited and re-issued to Vijay at ₹9 per share (face value ₹10). Calculate the profit on re-issue transferred to the Capital Reserve.
(A) 240
(B) 300
(C) 270
(D) 210

Ans :

(D) 210
The amount paid per share by Raja was ₹10 (face value) - ₹2 (unpaid final call) = ₹8. The total forfeited amount is 30 shares × ₹8 = ₹240. The discount on re-issue is ₹10 - ₹9 = ₹1 per share. The total discount is 30 shares × ₹1 = ₹30. The amount transferred to Capital Reserve is ₹240 (forfeited amount) - ₹30 (discount) = ₹210.

May/June 2019

88. Consider the following from a case study: "Prakash is allotted 100 shares which means his application must be for 150 (100 × 3/2) shares." The pro-rata ratio was 2 shares allotted for 3 shares applied.
Why was it necessary to calculate that Prakash applied for 150 shares?
(A) To calculate the excess application money paid by him, which is adjusted against allotment.
(B) To determine the total number of shareholders in the company.
(C) To calculate the premium amount due from him.
(D) To report the number of applied shares to the stock exchange.

Ans :

(A) To calculate the excess application money paid by him, which is adjusted against allotment. In a pro-rata allotment, calculating the number of shares applied for is crucial to determine the total application money paid. This allows the company to calculate the excess money paid (money for 150 shares minus money due for 100 shares) and adjust this surplus against the amount due from Prakash on allotment, thereby determining the actual allotment arrears.

Oct/Nov 2018

89. In a case study, Prakash was allotted 100 shares on a pro-rata basis. He paid ₹5 on application and failed to pay ₹4 on allotment. His excess application money adjusted was ₹250. What were his net allotment arrears?
(A) ₹400
(B) ₹250
(C) ₹150
(D) ₹650

Ans :

(C) ₹150
The total allotment money due on Prakash's 100 shares was 100 × ₹4 = ₹400. He had paid excess application money, which was calculated to be ₹250. This amount was adjusted against his allotment dues. Therefore, the net amount he failed to pay on allotment (his arrears) was ₹400 - ₹250 = ₹150.

May/June 2021

90. In a case study, Prakash's 100 shares were forfeited before the second call was made. The share value was ₹10, and the final call was ₹1. What was the called-up value per share at the time of his forfeiture?

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partnership firm lacks a separate legal identity, the law does not distinguish between the firm's debts and the partners' personal debts. Therefore, the partners are personally and fully liable for the firm's obligations.

May/June 2014

126. Consider the journal entry for the re-issue of a forfeited share from the text:

Bank a/c Dr. ₹80
Forfeited Shares a/c Dr. ₹60
To Share Capital a/c ₹100
To Capital Reserve a/c ₹40

What does this entry represent?

(A) A share of face value ₹100 was re-issued for ₹80, with a forfeited amount of ₹60, resulting in a ₹40 capital reserve.
(B) A share of face value ₹100 was forfeited, on which ₹60 was paid. It was then re-issued for ₹80, resulting in a capital profit of ₹40.
(C) A share of face value ₹140 was issued, and a capital reserve of ₹40 was created.
(D) A share was re-issued for ₹140, of which ₹100 went to share capital.

Ans :

(B) A share of face value ₹100 was forfeited, on which ₹60 was paid. It was then re-issued for ₹80, resulting in a capital profit of ₹40.
The entry shows that on re-issue, cash of ₹80 is received (Dr. Bank). The Forfeited Shares account is debited, meaning part of the previously forfeited amount is used. The total received by the company for the share is ₹60 (from old owner) + ₹80 (from new owner) = ₹140. Against a face value of ₹100, the excess of ₹40 is a capital profit.

Oct/Nov 2025

127. If a company's articles are silent, what is the maximum interest rate it can charge on Calls-in-Arrears?

(A) The chapter does not specify a rate for Calls-in-Arrears.
(B) 6% per annum
(C) 12% per annum
(D) 10% per annum

Ans :

(A) The chapter does not specify a rate for Calls-in-Arrears.
The provided text explicitly mentions that a company can pay interest on Calls-in-Advance up to a maximum of 6% per annum. However, it does not specify a corresponding interest rate that can be charged on Calls-in-Arrears. Therefore, based exclusively on the given content, this information is not available.

May/June 2019

128. In which situation would the Share Premium account be debited?

(A) When bonus shares are issued out of the share premium balance.
(B) When shares are issued at a price higher than their face value.
(C) When a dividend is paid out of the share premium account.
(D) When shares are re-issued at a premium.

Ans :

(A) When bonus shares are issued out of the share premium balance.
The Share Premium account is credited when shares are issued at a premium. It is debited when the balance is utilized for one of the legally permitted purposes. Issuing fully paid bonus shares is a valid use, and the journal entry involves debiting the Share Premium account to transfer the amount for the bonus issue.

Oct/Nov 2018

129. Which of the following is the most appropriate description of a 'Registered Company'?

(A) A company listed on a stock exchange.
(B) A company registered with SEBI for an IPO.
(C) A company registered under the provisions of the Companies Act.
(D) A company that has registered its trademark.

Ans :

(C) A company registered under the provisions of the Companies Act.
The term 'Registered Company' specifically refers to a company that has been incorporated and registered under the legal framework of the Companies Act (currently the 2013 Act or any previous company law). This registration is what grants it legal existence as a company. Examples include Tata Consultancy Services Ltd. and WIPRO Ltd.

May/June 2021

130. A company issues 1,000 shares of ₹100 each. It calls ₹60 per share. It receives ₹55 per share from holders of 900 shares and nothing from holders

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(B) ₹50,000
The Balance Sheet extract for Nilofar Ltd. clearly states the Authorised Capital as 5,000 Equity Shares of ₹10 each, which amounts to ₹50,000. This represents the maximum capital the company is authorized to raise, even though its current issued and paid-up capital is only ₹10,000.

May/June 2023

96. As per Section 43 of the Companies Act 2013, which of the following is NOT listed as a component of a company's share capital?
(A) Debentures with voting rights
(B) Equity shares with voting rights
(C) Equity shares with differential rights
(D) Preference share capital

Ans :

(A) Debentures with voting rights
Section 43 of the Companies Act 2013 specifies that the share capital of a company shall consist of equity shares (with voting rights or with differential rights) and preference share capital. Debentures are a form of debt, not share capital, and they do not carry voting rights.

Oct/Nov 2022

97. What is the main objective for a company to issue non-voting equity shares?
(A) To raise resources without diluting management control.
(B) To comply with international accounting standards.
(C) To give employees a greater say in company management.
(D) To reduce the company's dividend payment liability.

Ans :

(A) To raise resources without diluting management control.
The primary motivation for issuing non-voting equity shares is to raise capital from investors who are more interested in a higher dividend than in voting rights. This allows the existing management or promoters to raise funds without the risk of losing control over the company's decision-making processes.

May/June 2005

98. What is the maximum percentage of paid-up capital that can be issued as equity shares without voting rights?
(A) 10%
(B) 49%
(C) 25%
(D) 50%

Ans :

(C) 25%
A key condition for the issue of non-voting equity shares is that their total value cannot exceed 25% of the company's total paid-up capital. This cap ensures that a significant majority of the equity capital continues to hold voting rights, maintaining a balance in corporate governance and shareholder democracy.

Oct/Nov 2019

99. Which of the following conditions must be met to issue non-voting equity shares?
(A) The company must be a public company only.
(B) The issue must be approved by an ordinary resolution.
(C) The company's Articles of Association must authorize the issue.
(D) The dividend rate must be lower than that on voting shares.

Ans :

(C) The company's Articles of Association must authorize the issue.
One of the fundamental conditions for issuing non-voting equity shares is that the company's Articles of Association must contain a provision authorizing such an issue. Additionally, the issue requires approval from shareholders through a special resolution passed at a general body meeting, not just an ordinary resolution.

May/June 2012

100. Which of the following statements about non-voting equity shares is incorrect?
(A) Existing shares with voting rights can be converted into shares without voting rights.
(B) A special resolution must state the issue price and the higher dividend rate they carry.
(C) Both private and public companies can issue them.
(D) Holders of such shares are entitled to bonus shares.

Ans :

(A) Existing shares with voting rights can be converted into shares without voting rights.

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(A) ₹20 crores
(B) ₹25 crores
(C) ₹26.67 crores
(D) It cannot issue non-voting shares.

Ans :

(C) ₹26.67 crores
The 25% cap applies to the total paid-up capital after the new issue. Let 'x' be the value of new non-voting shares.
The new total paid-up capital will be (₹80 crores + x).
The condition is: $x \leq 0.25 \times (80 + x)$.
Solving for x: $x \leq 20 + 0.25x$, which gives $0.75x \leq 20$, so $x \leq 20/0.75$, or $x \leq 26.67$ crores.

May/June 2011

118. A company issues 10,000 shares of ₹10 each at a premium of ₹2 per share. The entire amount is payable on application. What is the journal entry for this transaction?
(A) Dr. Bank a/c ₹1,20,000; Cr. Share Application a/c ₹1,20,000
(B) Dr. Bank a/c ₹1,20,000; Cr. Share Capital a/c ₹1,00,000; Cr. Share Premium a/c ₹20,000
(C) Dr. Bank a/c ₹1,00,000; Cr. Share Capital a/c ₹1,00,000
(D) Dr. Bank a/c ₹1,20,000; Cr. Share Capital a/c ₹1,20,000

Ans :

(A) Dr. Bank a/c ₹1,20,000; Cr. Share Application a/c ₹1,20,000
When the money is first received, it is debited to the Bank account and credited to a temporary Share Application account. The segregation into Share Capital and Share Premium happens at the time of allotment. The total amount received is 10,000 shares × (₹10 + ₹2) = ₹1,20,000.

Oct/Nov 2020

119. Consider the 'Share Applications a/c' ledger.
The account is credited 'By Bank a/c' for ₹7,500. It is debited 'To Bank a/c' for ₹2,500 and 'To Share Capital a/c' for ₹5,000.
What do these entries signify?
(A) ₹7,500 was due, ₹2,500 was received, and ₹5,000 was forfeited.
(B) ₹5,000 was received, and ₹2,500 was paid as commission.
(C) ₹7,500 was received, ₹2,500 was refunded as excess, and ₹5,000 was transferred to share capital.
(D) ₹7,500 was received, all of which was transferred to share capital.

Ans :

(C) ₹7,500 was received, ₹2,500 was refunded as excess, and ₹5,000 was transferred to share capital.
The credit 'By Bank a/c' shows total application money received (1,500 applications x ₹5). The debit 'To Bank a/c' shows the refund for 500 excess applications (500 x ₹5). The debit 'To Share Capital a/c' shows the transfer of money for the 1,000 allotted shares (1,000 x ₹5) to the capital account.

May/June 2022

120. Which of the following is NOT a feature of a Government Company?
(A) It is managed directly by a ministry of the government.
(B) Not less than 51% of paid-up share capital is held by the Central Government.
(C) It can be partly owned by a State Government.
(D) It is defined under the Companies Act, 2013.

Ans :

(A) It is managed directly by a ministry of the government.
A Government Company is a company registered under the Companies Act and is managed by its own Board of Directors, even though the government holds a majority stake. It is not managed directly by a government ministry like a departmental undertaking. It maintains its separate legal and managerial structure.

Oct/Nov 2023

121. What is the fundamental difference between an 'Associate Company' and a 'Subsidiary Company'?
(A) A subsidiary is controlled by the holding company, while an associate is only significantly influenced.
(B) An associate company is one that holds over 50% of voting power, while a subsidiary holds less than 50%.
(C) An associate company is a legal term for a joint venture, whereas a subsidiary is an independent corporate entity.
(D) A subsidiary company can be a private company, but an associate company is required by law to be a public company.

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Oct/Nov 2015

105. Identify the correct statements regarding the issue of shares.

1. In case of oversubscription, a company can allot more shares than it offered.
2. Excess application money on pro-rata allotment is always refunded.
3. If minimum subscription is not received, allotment cannot proceed.
4. Application money is credited to the Share Capital account upon receipt.

(A) 1 and 4 only
(B) 3 only
(C) 2 and 3 only
(D) 1, 2, and 3

Ans :

(B) 3 only
Statement 1 is incorrect; a company cannot allot more shares than offered. Statement 2 is incorrect; excess money is usually adjusted against allotment. Statement 4 is incorrect; application money is credited to a temporary Share Applications account. Only statement 3 is correct; receiving minimum subscription is mandatory to proceed with share allotment.

May/June 2020

106. Match the item in List-I with the corresponding journal entry action in List-II.

List-I
P. Receipt of application money
Q. Allotment of shares
R. Forfeiture of shares
S. Re-issue of forfeited shares

List-II
1. Debit Share Capital Account
2. Credit Share Applications Account
3. Credit Capital Reserve Account
4. Debit Share Applications Account

(A) P-2, Q-4, R-1, S-3
(B) P-4, Q-2, R-3, S-1
(C) P-2, Q-1, R-4, S-3
(D) P-1, Q-4, R-2, S-3

Ans :

(A) P-2, Q-4, R-1, S-3
(P) On receipt of application money, Bank is debited and Share Applications is credited. (Q) On allotment, Share Applications is debited and Share Capital is credited. (R) On forfeiture, Share Capital is debited. (S) On re-issue, any profit is credited to the Capital Reserve account. This matching correctly aligns the actions.

Oct/Nov 2021

107. An extract on the utilization of share premium states:

"Premium amount can be utilised only for the following purposes: (a) Buy back of shares. (b) Issue of fully paid bonus shares. (c) Writing off preliminary expenses and discount or commission on issue of shares or debentures. (d) Paying premium on redemption of preference shares or debentures."

A company has a balance of ₹50 lakhs in its Share Premium account. Which of the following would be an invalid use of this fund?

(A) Paying ₹10 lakhs towards the premium payable on redemption of its debentures.
(B) Using ₹20 lakhs to issue fully paid bonus shares to its equity shareholders.
(C) Writing off ₹2 lakhs of underwriting commission paid on a recent share issue.
(D) Writing off an operating loss of ₹5 lakhs incurred in the current year.

Ans :

(D) Writing off an operating loss of ₹5 lakhs incurred in the current year.
The purposes for which share premium can be used are strictly defined by law. The list includes bonus issues, buy-backs, writing off specific capital expenses, and paying redemption premiums. Writing off a normal business or operating loss is not a permitted use of the share premium account, as it is a capital receipt.

May/June 2013

108. Which of the following statements about 'Calls in Advance' is incorrect?

(A) It is treated as part of the paid-up share capital from the date of receipt.
(B) The company may accept them if its Articles permit.
(C) Interest can be paid on this amount, not exceeding 6% p.a.
(D) It is adjusted against the respective call when it becomes due.

Ans :

(A) It is treated as part of the paid-up share capital from the date of receipt.
Calls in Advance are not part of the paid-up capital until the actual call is made by the

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The rules explicitly state that no company will be permitted to convert its existing shares with voting rights into shares without voting rights. This prevents companies from retrospectively disenfranchising their existing shareholders. New non-voting shares must be issued as a separate class of shares from the outset.

Oct/Nov 2006

101. **Assertion (A) :** A company is an artificial person created by law.
Reason (R) : The death or insolvency of a shareholder affects the existence of the company.
(A) Both A and R are true and R is the correct explanation of A.
(B) Both A and R are true but R is not the correct explanation of A.
(C) A is true but R is false.
(D) A is false but R is true.

Ans :

(C) A is true but R is false.
Assertion (A) is true; a company is legally recognized as an artificial person. Reason (R) is false. A key feature of a company is 'perpetual succession', which means its existence is not affected by the death or insolvency of its members. The company continues to exist until legally wound up.

May/June 2025

102. Statement I: The shares of a private limited company are freely transferable.
Statement II : A private limited company prohibits any invitation to the public to subscribe for any of its securities.
(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Statement I is correct, but Statement II is incorrect.
(D) Statement I is incorrect, but Statement II is correct.

Ans :

(D) Statement I is incorrect, but Statement II is correct.
Statement I is incorrect because a private company, by its articles, restricts the right to transfer its shares. Statement II is correct as it is a defining characteristic of a private company that it cannot invite the public to subscribe to its shares or debentures, limiting its fundraising to private sources.

Oct/Nov 2005

103. Consider the following statements about preference shares:
1. They have a preferential right to dividend payment over equity shares.
2. The dividend rate on preference shares is not fixed.
3. They have a preferential right to the return of capital in the event of winding up.

Which of the above statements is/are correct?
(A) 1 only
(B) 1 and 3 only
(C) 2 and 3 only
(D) 1, 2, and 3

Ans :

(B) 1 and 3 only
Preference shares are characterized by two primary preferential rights. They are entitled to receive dividends at a fixed rate before any dividend is paid to equity shareholders. They also have priority in the repayment of their capital during the company's winding up. The dividend rate is typically fixed, making statement 2 incorrect.

May/June 2010

104. Which of the following pairs is incorrectly matched?
(A) Authorised Capital: Maximum capital a company can raise.
(B) Issued Capital: Part of authorised capital offered to the public.
(C) Called-up Capital: Amount actually paid by shareholders.
(D) Subscribed Capital: Part of issued capital taken up by the public.

Ans :

(C) Called-up Capital: Amount actually paid by shareholders.
This pair is incorrectly matched. Called-up Capital is the amount that the company has demanded from shareholders, not the amount they have actually paid. The amount actually paid by shareholders is known as 'Paid-up Capital'. Paid-up capital can be less than or equal to called-up capital, but not more.

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Therefore, three statements (1, 3, and 5) are correct, while two are incorrect.

Oct/Nov 2013

113. A company forfeited 100 shares of ₹10 each, on which ₹7 per share was called up. The shareholder had paid only the application money of ₹2 per share. What amount will be debited to the Share Capital account?
(A) ₹1,000
(B) ₹700
(C) ₹500
(D) ₹200

Ans :

(B) ₹700
The forfeiture entry requires the Share Capital account to be debited with the called-up amount on the forfeited shares, not the face value or the paid-up amount. In this case, the called-up amount is ₹7 per share. For 100 shares, the total amount to be debited to the Share Capital account is 100 × ₹7 = ₹700.

May/June 2008

114. Following the forfeiture in the previous question (100 shares of ₹10, ₹7 called-up, ₹2 paid), the company re-issued all 100 shares as '₹7 paid-up' for a price of ₹6 per share. What is the amount transferred to Capital Reserve?
(A) ₹100
(B) ₹200
(C) ₹500
(D) Nil

Ans :

(A) ₹100
The amount forfeited per share is ₹2. For 100 shares, the total forfeited amount is ₹200. The shares are re-issued as ₹7 paid-up for ₹6, which means a discount of ₹1 per share is allowed on re-issue. The total discount is 100 × ₹1 = ₹100. The amount transferred to Capital Reserve is Forfeited Amount - Discount = ₹200 - ₹100 = ₹100.

Oct/Nov 2014

115. Consider the table showing the types of companies.
(A) Based on Incorporation: Chartered, Statutory, Registered, Foreign
(B) Based on Ownership: Private, Public, Government, Holding
(C) Based on Liability: Limited by Shares, Limited by Guarantee, Unlimited Liability, Subsidiary
Which category contains an incorrectly placed company type?
(A) Category (A)
(B) Category (B)
(C) Category (C)
(D) All categories are correct.

Ans :

(C) Category (C)
The table classifies companies based on Incorporation, Ownership, and Liability. In Category (C) Based on Liability, 'Subsidiary Company' is incorrectly placed. A subsidiary company is defined by its relationship of control with a holding company, which is a classification based on ownership, not liability. The other types in Category (C) are correctly based on liability.

May/June 2015

116. Statement I: A company with unlimited liability can be incorporated with or without share capital.
Statement II : A company limited by guarantee is generally a non-profit making organisation.
(A) Both Statement I and Statement II are correct.
(B) Both Statement I and Statement II are incorrect.
(C) Statement I is correct, but Statement II is incorrect.
(D) Statement I is incorrect, but Statement II is correct.

Ans :

(A) Both Statement I and Statement II are correct.
Both statements are factually correct. The law allows for the incorporation of an unlimited company with or without share capital. Similarly, companies limited by guarantee are typically formed for the promotion of non-commercial objectives like art, science, or charity, and are essentially non-profit making entities.

Oct/Nov 2012

117. An excerpt on non-voting shares states: "Only 25 per cent of the paid-up capital of the company can be issued as equity shares without voting rights."
A company has a total paid-up capital of ₹80 crores, consisting entirely of equity shares with voting rights. What is the maximum value of new non-voting equity shares it can issue?

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(A) ₹10
(B) ₹8
(C) ₹9
(D) ₹7

Ans :

(C) ₹9
The total face value is ₹10. The instalments are Application (₹3 face value + ₹2 premium), Allotment (₹4), 1st Call (₹2), and Final Call (₹1). Prakash's shares were forfeited after the 1st call but before the final call of ₹1 was made. Therefore, the called-up capital per share is ₹10 - ₹1(uncalled) = ₹9.

Oct/Nov 2024

91. In a case study, Dinesh, who was allotted 200 shares, failed to pay the 1st call (₹2) and final call (₹1). His shares were forfeited after the final call. What is the total amount of his calls in arrear?
(A) ₹200
(B) ₹400
(C) ₹600
(D) ₹950

Ans :

(C) ₹600
Dinesh failed to pay two calls on his 200 shares. The amount due on the 1st Call was 200 × ₹2 = ₹400. The amount due on the Final Call was 200 × ₹1 = ₹200. His total calls in arrear at the time of forfeiture are the sum of these two amounts, which is ₹400 + ₹200 = ₹600.

May/June 2017

92. 200 forfeited shares were re-issued at ₹5 per share (face value ₹10). These included 100 shares on which ₹550 had been forfeited, and 100 shares on which ₹700 had been forfeited. What is the total amount transferred to Capital Reserve?
(A) ₹1,250
(B) ₹1,000
(C) ₹250
(D) ₹500

Ans :

(C) ₹250
Total forfeited amount on 200 re-issued shares is ₹550 + ₹700 = ₹1,250. The total face value of re-issued shares is 200 × ₹10 = ₹2,000. The amount received on re-issue is 200 × ₹5 = ₹1,000. The discount on re-issue is ₹2,000 - ₹1,000 = ₹1,000. Capital Reserve = Forfeited Amount - Discount = ₹1,250 - ₹1,000 = ₹250.

Oct/Nov 2009

93. Nilofar Ltd. issued 1,000 shares, received applications for 1,500, and returned the excess application money. If application money was ₹5 per share, what is the amount refunded to applicants?
(A) ₹7,500
(B) ₹5,000
(C) ₹2,500
(D) ₹1,000

Ans :

(C) ₹2,500
The company received applications for 1,500 shares but only allotted 1,000 shares. The excess applications are 1,500 - 1,000 = 500. Since the excess money was returned, the amount refunded is the number of excess applications multiplied by the application money per share, which is 500 × ₹5 = ₹2,500.

May/June 2016

94. Based on the ledger accounts for Nilofar Ltd. from Question 93, what is the closing balance of the Bank account after all transactions are completed?
(A) ₹12,500
(B) ₹15,000
(C) ₹10,000
(D) ₹7,500

Ans :

(C) ₹10,000
The Bank account was debited with total receipts: ₹7,500 (Application), ₹3,000 (Allotment), and ₹2,000 (Final Call), totaling ₹12,500. It was credited with the refund of excess application money, which was ₹2,500. The closing balance is therefore ₹12,500 - ₹2,500 = ₹10,000, which matches the company's final paid-up capital.

Oct/Nov 2010

95. According to the Balance Sheet extract of Nilofar Ltd., what is the value of Authorised Capital?
(A) ₹10,000
(B) ₹50,000
(C) ₹1,000
(D) ₹12,500

Ans :

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Ans :

(A) A subsidiary is controlled by the holding company, while an associate is only significantly influenced.
The key difference lies in the level of control. A company becomes a subsidiary when the holding company has control (e.g., controls board composition or over half the share capital). It is an associate company when the other company has 'significant influence' but not outright control, which is a lower threshold of power.

May/June 2018

122. As per the SEBI guidelines for bonus issues, "A company which announces its bonus issue after the approval of the board of directors and does not require shareholders' approval... shall implement the bonus issue within fifteen days from the date of such approval and shall not have the option of changing the decision."
What is the implication of this guideline?
(A) All bonus issues must be completed within 15 days.
(B) The 15-day timeline applies only after shareholder approval is obtained.
(C) Board-approved bonus issues that don't need shareholder consent are irrevocable and must be executed quickly.
(D) Companies can change their decision on a bonus issue anytime before the record date.

Ans :

(C) Board-approved bonus issues that don't need shareholder consent are irrevocable and must be executed quickly.
This specific guideline applies to situations where the Articles of Association empower the Board to issue bonus shares without going to the shareholders. In such cases, once the Board approves the issue, the decision becomes binding, and the company must implement it within the short timeframe of 15 days.

Oct/Nov 2016

123. A company forfeited 50 shares of ₹10 each, fully called up. The shareholder had failed to pay the first call of ₹3 and the final call of ₹2. The shares were re-issued at ₹8 per share as fully paid-up. Calculate the gain on re-issue.
(A) ₹150
(B) ₹250
(C) ₹400
(D) ₹100

Ans :

(A) ₹150
The amount paid per share was ₹10 - (₹3 + ₹2) = ₹5. Total amount forfeited is 50 × ₹5 = ₹250. The discount on re-issue is ₹10 - ₹8 = ₹2 per share. Total discount is 50 × ₹2 = ₹100. The gain on re-issue transferred to Capital Reserve is the forfeited amount minus the discount, i.e., ₹250 - ₹100 = ₹150.

May/June 2007

124. What is the primary purpose of debiting the Share Allotment account when allotment money becomes due?
(A) To record the receipt of cash from shareholders.
(B) To create a receivable from the shareholders for the amount due on allotment.
(C) To transfer the application money to the allotment account.
(D) To write off the expenses related to the share issue.

Ans :

(B) To create a receivable from the shareholders for the amount due on allotment.
When the Board of Directors makes the allotment, an amount becomes legally due from the allottees. To record this, the Share Allotment account is debited, creating an asset (a receivable), and the Share Capital account is credited. The subsequent receipt of cash will then be credited against this receivable.

Oct/Nov 2007

125. **Assertion (A) :** The liability of partners in a partnership firm is unlimited.
Reason (R) : A partnership firm is not considered a separate legal entity from its partners.
(A) Both A and R are true and R is the correct explanation of A.
(B) Both A and R are true but R is not the correct explanation of A.
(C) A is true but R is false.
(D) A is false but R is true.

Ans :

(A) Both A and R are true and R is the correct explanation of A.
The assertion is true. The reason is also true and correctly explains the assertion. Because a

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company. Until then, it is treated as a liability of the company to the shareholder and is shown separately in the balance sheet. It only becomes part of the paid-up capital when the call is due and adjusted.

Oct/Nov 2008

109. What is the chronological order of the following events in a share issue process?

1. Receipt of application money
2. Allotment of shares
3. Making the first call
4. Issue of prospectus

(A) 4, 1, 2, 3
(B) 1, 4, 2, 3
(C) 4, 2, 1, 3
(D) 1, 2, 3, 4

Ans :

(A) 4, 1, 2, 3
The correct sequence begins with the company issuing a prospectus to invite the public (4). Based on this, the company receives applications and the corresponding money (1). The Board of Directors then finalizes the allotment of shares (2). Subsequently, the company makes calls for the remaining amount, such as the first call (3).

May/June 2024

110. **Assertion (A) :** A company cannot issue shares at a discount.
Reason (R) : Section 54 of the Companies Act, 2013, allows the issue of sweat equity shares at a discount.

(A) Both A and R are true and R is the correct explanation of A.
(B) Both A and R are true but R is not the correct explanation of A.
(C) A is true but R is false.
(D) A is false but R is true.

Ans :

(B) Both A and R are true but R is not the correct explanation of A.
Assertion (A) states the general rule from Section 53, which is true. Reason (R) states the specific exception to this rule provided in Section 54, which is also true. However, R is an exception to A, not the explanation for why the general rule exists. The reason for the rule is to prevent capital erosion.

Oct/Nov 2017

111. An extract from the Companies Act, 2013 states: "A company may issue preference shares which are liable to be redeemed within a period not exceeding twenty years from the date of their issue... Provided that a company may issue preference shares for a period exceeding twenty years but not exceeding thirty years for infrastructure projects..."
Based on this, which of the following issues is permissible?

(A) A software company issuing irredeemable preference shares.
(B) A manufacturing company issuing preference shares redeemable after 25 years.
(C) An infrastructure company issuing preference shares redeemable after 28 years.
(D) Any company issuing preference shares redeemable after 35 years.

Ans :

(C) An infrastructure company issuing preference shares redeemable after 28 years.
The rule prohibits irredeemable shares. The general maximum redemption period is 20 years. A manufacturing company is bound by this 20-year limit, so 25 years is not allowed. However, the proviso allows infrastructure companies a longer period, up to 30 years. Therefore, an issue redeemable after 28 years by an infrastructure company is permissible.

May/June 2006

112. Consider the features of a joint stock company:

1. It has a separate legal status.
2. The liability of members is unlimited.
3. The use of a common seal is now optional.
4. It does not have perpetual succession.
5. Management is separated from ownership.

How many of the above statements are correct?

(A) Two
(B) Three
(C) Four
(D) Five

Ans :

(B) Three
Statement 1 is correct. Statement 2 is incorrect; liability is limited. Statement 3 is correct as per the 2015 amendment. Statement 4 is incorrect; it has perpetual succession. Statement 5 is correct.

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of 100 shares. What is the amount of Paid-up Capital?
(A) ₹49,500
(B) ₹60,000
(C) ₹54,000
(D) ₹55,000

Ans :

(A) ₹49,500
Paid-up capital is the amount actually received from shareholders against the called-up amount. In this case, the company received ₹55 per share from the holders of 900 shares. Therefore, the total paid-up capital is the amount received, which is calculated as 900 shares × ₹55/share = ₹49,500. The amount not received does not form part of paid-up capital.

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(C) Other current liabilities
The guidelines for 'Other current liabilities' are very specific about this. Share application money received that is due for refund, for instance, when minimum subscription is not met, shall be separately shown under 'Other current liabilities'. This is because it represents a current obligation to refund the money to applicants.

May/June 2018

28. In the classification of Tangible Assets, which of the following is NOT listed as a separate class?
(A) Land
(B) Buildings
(C) Office Equipment
(D) Inventory

Ans :

(D) Inventory
The schedule lists specific classes under 'Tangible assets' such as Land, Buildings, Plant and Equipment, Furniture and Fixtures, Vehicles, and Office equipment. Inventory is not a tangible fixed asset; it is a separate line item under 'Current Assets' and represents goods held for sale or use in production.

Oct/Nov 2016

29. For how many years subsequent to a revaluation of assets must a company show the increased or reduced figures and disclose the amount of the increase or decrease in a note?
(A) For the first year only
(B) For the first two years
(C) Five years
(D) For the entire life of the asset

Ans :

(C) Five years
The disclosure requirement following a revaluation is time-bound. It states that for the first five years subsequent to the date of revaluation (or reduction of capital affecting asset values), every balance sheet must show the adjusted figures and also disclose the amount of the increase or decrease and the date it occurred via a note.

May/June 2014

30. Which of the following items is classified as an 'Intangible asset' under Schedule III?
(A) Investment Property
(B) Goodwill
(C) Deferred Tax Asset
(D) Security Deposits

Ans :

(B) Goodwill
Schedule III provides a detailed list for the classification of intangible assets. This list explicitly includes Goodwill, Brands/trademarks, Computer software, Mastheads and publishing titles, Mining rights, Copyrights, patents, and other similar items. Investment Property, Deferred Tax Assets, and Security Deposits are classified under different asset heads.

Oct/Nov 2007

31. Under the heading 'Non-current investments', which of the following is NOT a specified classification?
(A) Investments in Mutual Funds
(B) Investments in Equity Instruments
(C) Investments in commercial property for own use
(D) Investments in Government or trust securities

Ans :

(C) Investments in commercial property for own use
Commercial property for a company's own use would be classified as a Tangible Asset (e.g., Buildings) and not an investment. The 'Non-current investments' category includes 'Investment property' (held to earn rentals or for capital appreciation), as well as investments in various financial instruments like equity, preference shares, mutual funds, and government securities.

May/June 2025

32. What specific disclosure is required for investments in partnership firms?
(A) Only the aggregate amount of investment.
(B) The names of the firms and the expected rate of return.
(C) The names of the firms, names of all partners, total capital, and the share of each partner.
(D) A valuation report from an independent chartered accountant for the firm.

Ans :

(C) The names of the firms, names of all partners, total capital, and the share of each partner.

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not include the cash flow statement, making it optional for these specific types of entities.

Oct/Nov 2023

5. According to the General Instructions of Schedule III, if compliance with the Companies Act or applicable Accounting Standards necessitates a change in the treatment or disclosure in the financial statements, what is the consequence?

(A) The company must seek approval from the Tribunal before making the change.
(B) The requirements of Schedule III will override the Accounting Standards.
(C) The change shall be made, and the requirements of Schedule III shall stand modified accordingly.
(D) The company must only disclose the deviation in the notes to accounts without changing the format.

Ans :

(C) The change shall be made, and the requirements of Schedule III shall stand modified accordingly.
The first general instruction of Schedule III is clear on this matter. It states that where compliance with the Act or Accounting Standards requires any change, inter se, in the financial statements, the same shall be made. Consequently, the requirements of the Schedule are considered to be modified to accommodate such necessary changes for true and fair reporting.

May/June 2007

6. What is the primary purpose of 'Notes to accounts' as described in Schedule III of the Companies Act, 2013?

(A) To provide a detailed summary of the company's business strategy and market outlook for the upcoming year.
(B) To provide narrative descriptions or disaggregations of items recognised in the financial statements.
(C) To list the full names, addresses, and qualifications of the company's board of directors and key personnel.
(D) To serve as a complete replacement for the cash flow statement for small and one-person companies.

Ans :

(B) To provide narrative descriptions or disaggregations of items recognised in the financial statements.
As per Schedule III, notes to accounts are meant to contain information in addition to what is presented in the financial statements. They provide required narrative descriptions, disaggregations of items recognized in those statements, and also information about items that do not qualify for recognition, thereby enhancing clarity and understanding for the users of these statements.

Oct/Nov 2018

7. According to Schedule III, how should a company with a turnover of ₹150 crores round off the figures appearing in its Financial Statements?

(A) To the nearest hundreds, thousands, lakhs, or millions.
(B) To the nearest thousands, lakhs, millions, or crores.
(C) Rounding off is not permitted for companies with turnover above ₹100 crores.
(D) To the nearest lakhs, millions, or crores, or decimals thereof.

Ans :

(D) To the nearest lakhs, millions, or crores, or decimals thereof.
The rules for rounding off are based on turnover. For a company with a turnover of one hundred crore rupees or more, the figures in the financial statements may be rounded off to the nearest lakhs, millions, or crores, or decimals thereof. This allows for a cleaner presentation of large financial figures in the statements.

May/June 2015

8. What is the rule regarding the presentation of comparative amounts in the financial statements as per Schedule III?

(A) Comparative amounts for the immediately preceding reporting period must be given for all items.
(B) Comparative amounts are required only for items on the Balance Sheet.
(C) Comparative amounts are optional and can be included at the discretion of the management.
(D) Comparative amounts are only required if the company's profit has increased by more than 10 %.

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Ans :

(B) A liability for goods purchased or services received in the normal course of business.
The definition provided in the notes to the Balance Sheet format is specific. A payable is classified as a "trade payable" if it is in respect of the amount due on account of goods purchased or services received in the normal course of business. This distinguishes it from other payables like loans or statutory dues.

May/June 2011

18. Which of the following details regarding share capital is NOT a required disclosure in the notes to accounts?
(A) The closing market price of the company's shares on a recognised stock exchange as at the balance sheet date.
(B) A reconciliation of outstanding shares from the beginning to the end of the period.
(C) The designated par value for each class of share.
(D) Details of shareholders holding more than 5 % of shares.

Ans :

(A) The closing market price of the company's shares on a recognised stock exchange as at the balance sheet date.
The detailed disclosure requirements for share capital are extensive, including authorised/ issued/subscribed capital, a reconciliation of shares, par value, rights attached to shares, and significant shareholdings. However, disclosing the market price of the shares on the balance sheet date is not a mandated requirement within these specific notes as per the provided text.

Oct/Nov 2012

19. For what period immediately preceding the Balance Sheet date must a company disclose the aggregate number and class of shares allotted as bonus shares?
(A) One year
(B) Two years
(C) Five years
(D) Three years

Ans :

(C) Five years
The disclosure requirements for share capital mandate a look-back period for certain events. For the period of five years immediately preceding the date of the Balance Sheet, the company must disclose the aggregate number and class of shares allotted as fully paid-up by way of bonus shares, as well as shares bought back.

May/June 2016

20. Which of the following is NOT classified under 'Reserves and Surplus' in the notes to the Balance Sheet?
(A) Forfeited shares account
(B) Capital Redemption Reserve
(C) Share Options Outstanding Account
(D) Revaluation Reserve

Ans :

(A) Forfeited shares account
The amount originally paid-up on forfeited shares is required to be disclosed under the 'Share Capital' note. 'Reserves and Surplus' includes specific items like Capital Reserve, Capital Redemption Reserve, Securities Premium Reserve, Debenture Redemption Reserve, Revaluation Reserve, and Share Options Outstanding Account, but not the forfeited shares amount itself.

Oct/Nov 2019

21. What is the term used for a reserve that is specifically represented by earmarked investments?
(A) A Surplus
(B) A Provision
(C) A Sinking Reserve
(D) A Fund

Ans :

(D) A Fund
The notes on 'Reserves and Surplus' provide a specific definition. It states that a reserve which is specifically represented by earmarked investments shall be termed as a "fund". This distinguishes it from general reserves which are not backed by specific, segregated investments and are just an appropriation of profit.

May/June 2005

22. How should a debit balance (loss) in the Statement of Profit and Loss be shown in the Balance Sheet?
(A) As a specific deduction from the total of 'Other current assets' on the asset side.
(B) As a negative amount under the 'Surplus' line item within Reserves and Surplus.
(C) As a contingent liability disclosed within the

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provisions, which are obligations not expected to be settled within the normal operating cycle.

Oct/Nov 2006

13. Under which main heading in the Assets side of the Schedule III Balance Sheet would you find 'Capital work-in-progress'?
(A) Current assets
(B) Non-current investments
(C) Fixed assets
(D) Other non-current assets

Ans :

(C) Fixed assets
'Capital work-in-progress' is shown as a sub-item under the broader category of 'Fixed assets', which falls under the main heading 'Non-current assets'. This classification is logical as it represents expenditure on tangible assets that are still under construction or development and are not yet ready for their intended use in the business.

May/June 2024

14. Identify the correct statement regarding the classification of an asset as 'current' according to the general instructions for the preparation of a Balance Sheet.
(A) An asset is current only if it is cash or a cash equivalent.
(B) An asset is current if it is expected to be realised within 24 months after the reporting date.
(C) All intangible assets are classified as non-current by default.
(D) An asset is current if it is expected to be realised in the company's normal operating cycle.

Ans :

(D) An asset is current if it is expected to be realised in the company's normal operating cycle. The instructions provide four criteria for classifying an asset as current, and satisfying any one is sufficient. One key criterion is that the asset is expected to be realised in, or is intended for sale or consumption in, the company's normal operating cycle. The other criteria relate to trading, realisation within twelve months, or being cash/cash equivalent.

Oct/Nov 2017

15. What is the assumed duration of a company's normal operating cycle if it cannot be identified?
(A) Twelve months
(B) Six months
(C) Eighteen months
(D) Twenty-four months

Ans :

(A) Twelve months
The general instructions for preparing the Balance Sheet state that an operating cycle is the time between acquiring assets for processing and their realisation in cash. Crucially, where the normal operating cycle cannot be identified, it is assumed to have a duration of twelve months for the purpose of classifying assets and liabilities.

May/June 2008

16. A liability is classified as 'current' if it satisfies any of the specified criteria. Which of the following is NOT one of those criteria?
(A) It is expected to be settled in the company's normal operating cycle.
(B) The company has an unconditional right to defer its settlement for at least twelve months.
(C) It is due to be settled within twelve months after the reporting date.
(D) It is held primarily for the purpose of being traded.

Ans :

(B) The company has an unconditional right to defer its settlement for at least twelve months.
The absence of an unconditional right to defer settlement for at least twelve months is a condition for classifying a liability as current. Conversely, if a company does have such an unconditional right, the liability would be classified as non-current. The other options are valid criteria for a current liability classification.

Oct/Nov 2020

17. How is a 'trade payable' defined in the general instructions of Schedule III?
(A) Any liability, regardless of its origin, that is payable by the company within twelve months.
(B) A liability for goods purchased or services received in the normal course of business.
(C) Any short-term borrowing from a bank or financial institution used to finance daily operations.
(D) An amount payable to directors, key management personnel, or other related parties of the company.

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Ans :

(A) Comparative amounts for the immediately preceding reporting period must be given for all items.
Except for the very first financial statements after incorporation, the general instructions mandate the presentation of corresponding amounts for the immediately preceding reporting period. This applies to all items shown in the financial statements, including the notes, to allow for meaningful comparison and trend analysis by the users of the statements.

Oct/Nov 2009

9. What is the standard financial year for a company or body corporate as defined in Schedule III of the Companies Act, 2013?
(A) The period ending on the 31st day of December every year.
(B) Any 12-month period as decided by the company's Board of Directors.
(C) The period ending on the 31st day of March every year.
(D) The period from 1st July to 30th June of the following year.

Ans :

(C) The period ending on the 31st day of March every year.
Schedule III defines the "Financial year" in relation to any company or body corporate as the period ending on the 31st day of March every year. An exception exists for companies incorporated on or after the 1st of January, where their first financial year extends to the 31st of March of the following year.

May/June 2019

10. Under what circumstance can a company, which is a holding or subsidiary of a company incorporated outside India, apply to the Tribunal to follow a different financial year?
(A) If required to align its financial year for consolidating accounts outside India.
(B) If the foreign parent company is listed on a major international stock exchange like the NYSE or LSE.
(C) If the company's primary business operations, representing over 75 % of revenue, are conducted outside of India.
(D) If the company's turnover from exports consistently exceeds 50 % of its total turnover for three consecutive years.

Ans :

(A) If required to align its financial year for consolidating accounts outside India.
A proviso allows a company or body corporate, which is a holding company or a subsidiary of a company incorporated outside India, to apply to the Tribunal. If the Tribunal is satisfied that the company needs to follow a different financial year for consolidating its accounts outside India, it may allow a different period as its financial year.

Oct/Nov 2022

11. In the prescribed format of the Balance Sheet under Schedule III, 'Money received against Share Warrants' is classified under which major head?
(A) Current Liabilities
(B) Non-current liabilities
(C) Share application money pending allotment
(D) Shareholders' funds

Ans :

(D) Shareholders' funds
According to Part I of Schedule III, the format of the Balance Sheet classifies 'Money received against Share Warrants' as a component of 'Shareholders' funds'. This head also includes Share Capital and Reserves and Surplus, representing the total equity interest of the owners in the company. It is placed just below these two items.

May/June 2013

12. Which of the following is NOT a sub-head under 'Non-current liabilities' in the Schedule III Balance Sheet format?
(A) Long-term borrowings
(B) Trade payables
(C) Deferred tax liabilities (Net)
(D) Long-term provisions

Ans :

(B) Trade payables
In the prescribed format of the Balance Sheet, 'Trade payables' are classified as a sub-head under the major head 'Current liabilities'. Non-current liabilities include items such as Long-term borrowings, Deferred tax liabilities (Net), Other Long term liabilities, and Long-term

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notes to the financial accounts.
(D) It should be directly netted off against the paid-up 'Share Capital' amount in equity.

Ans :

(B) As a negative amount under the 'Surplus' line item within Reserves and Surplus.
The instructions clearly state that a debit balance of the statement of profit and loss shall be shown as a negative figure under the head "Surplus". This negative balance is then adjusted against the total of other reserves, and the net figure is shown under the main head "Reserves and Surplus".

Oct/Nov 2011

23. Which of the following is NOT a classification of 'Long-term borrowings' as per Schedule III?
(A) Bonds/debentures
(B) Deposits
(C) Commercial Papers
(D) Loans and advances from related parties

Ans :

(C) Commercial Papers
Commercial Papers are typically short-term money market instruments. The classification for 'Long-term borrowings' includes items like Bonds/debentures, Term loans, Deferred payment liabilities, Deposits, and Loans from related parties. Short-term borrowings would be the more appropriate category for instruments like Commercial Papers.

May/June 2017

24. When disclosing bonds/debentures, in what order should they be stated?
(A) In ascending order based on their stated coupon or interest rate.
(B) In ascending order of maturity, with the nearest maturity date listed first.
(C) In alphabetical order according to the name of the debenture or bond series.
(D) In descending order of maturity or conversion date.

Ans :

(D) In descending order of maturity or conversion date.
The disclosure requirement for bonds and debentures is specific. They must be stated in descending order of maturity or conversion, starting from the farthest redemption or conversion date. This provides users with a clear view of the long-term repayment schedule, beginning with the obligations that are due furthest in the future.

Oct/Nov 2025

25. Under which head would a company classify 'Provision for employee benefits' that are not expected to be settled within 12 months?
(A) Long-term provisions
(B) Short-term provisions
(C) Other current liabilities
(D) Other long-term liabilities

Ans :

(A) Long-term provisions
The schedule provides a clear classification for provisions. 'Long-term provisions' are to be classified into 'Provision for employee benefits' and 'Others'. This category is used for obligations like gratuity or leave encashment where the settlement is expected to occur beyond the company's normal operating cycle or twelve months from the reporting date.

May/June 2012

26. Which of the following is classified under 'Short-term borrowings'?
(A) Long term maturities of finance lease obligations
(B) Loans repayable on demand from banks
(C) Debentures redeemable after 5 years
(D) Deferred payment liabilities

Ans :

(B) Loans repayable on demand from banks
'Short-term borrowings' include liabilities that are due within the operating cycle or 12 months. 'Loans repayable on demand' from banks or other parties fit this description perfectly. The other options, such as long-term maturities, debentures with a 5-year term, and deferred liabilities, are all examples of non-current or long-term liabilities.

Oct/Nov 2010

27. Share application money that is due for refund because minimum subscription requirements were not met is shown under which heading?
(A) Shareholders' funds
(B) Share application money pending allotment
(C) Other current liabilities
(D) Short-term provisions

Ans :

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typically includes cash on hand, balances with banks, and cheques or drafts on hand, which are readily convertible to cash.

May/June 2023

38. Under which heading are 'Guarantees' given by the company disclosed?
(A) Long-term provisions
(B) Other non-current liabilities
(C) Contingent liabilities and commitments
(D) Other current liabilities

Ans :

(C) Contingent liabilities and commitments
Guarantees represent a potential future obligation that depends on the outcome of an uncertain event (i.e., the default of the party for whom the guarantee was given). Therefore, they are not recognized as a liability on the balance sheet but are disclosed in the notes under 'Contingent liabilities and commitments'.

Oct/Nov 2008

39. A company issues securities for the specific purpose of building a new factory. If the amount is not fully used by the balance sheet date, what disclosure is required?
(A) A note indicating how the unutilised amounts have been used or invested.
(B) The unutilised amount must be transferred to the Capital Reserve.
(C) The unutilised amount must be shown as a short-term borrowing.
(D) No special disclosure is required until the project is complete.

Ans :

(A) A note indicating how the unutilised amounts have been used or invested.
To ensure accountability for funds raised for a specific purpose, the schedule mandates a disclosure. Where money from an issue of securities has not been fully used for its intended purpose, a note must indicate how such unutilised amounts have been temporarily used or where they have been invested pending their final application.

May/June 2006

40. In the format of the Statement of Profit and Loss, what is the formula to arrive at 'Profit before exceptional and extraordinary items and tax'?
(A) Total Revenue (I+II) - Total expenses (IV)
(B) Total Revenue (I+II) + Total expenses (IV)
(C) Total Revenue (I+II) - Finance costs
(D) Revenue from operations (I) - Total expenses (IV)

Ans :

(A) Total Revenue (I+II) - Total expenses (IV)
The vertical format of the Statement of Profit and Loss is structured logically. It first calculates Total Revenue (Revenue from operations + Other income). Then, it aggregates all operational expenses. The profit before considering any exceptional or extraordinary items and tax is calculated as Total Revenue (Item III) minus Total expenses (Item IV).

Oct/Nov 2013

41. In the Statement of Profit and Loss, which two components are deducted from 'Profit before extraordinary items and tax (V-VI)' to arrive at 'Profit (Loss) for the period from continuing operations'?
(A) Exceptional items and Extraordinary items
(B) Exceptional items and Finance costs
(C) Finance costs and Depreciation
(D) Extraordinary items and Tax expense

Ans :

(D) Extraordinary items and Tax expense
The P&L statement format follows a clear sequence. 'Profit before extraordinary items and tax' is line item VII. From this, 'Extraordinary items' (VIII) are deducted to get 'Profit before tax' (IX). Then, 'Tax expense' (X) is deducted. The resulting figure, 'Profit (Loss) for the period from continuing operations' (XI), is calculated as VII - VIII - X.

May/June 2022

42. For a company that is not a finance company, how is 'Revenue from operations' disclosed?
(A) As a single line item without any breakdown.
(B) Separately disclosing revenue from Sale of products, Sale of services, and Other operating revenues, less Excise duty.
(C) Separately disclosing Interest income and Other financial services income.
(D) As a net figure after deducting all direct costs of operation.

Ans :

NODIA

The disclosure requirements for investments are very detailed. In regard to investments in the capital of partnership firms, the schedule mandates the disclosure of the names of the firms, the names of all their partners, the total capital of the firm, and the shares of each partner, providing complete transparency.

Oct/Nov 2024

33. Under 'Long-term loans and advances', how are the amounts sub-classified?
(A) Domestic and Foreign
(B) Quoted and Unquoted
(C) Secured, considered good; Unsecured, considered good; and Doubtful
(D) To related parties and to third parties

Ans :

(C) Secured, considered good; Unsecured, considered good; and Doubtful
The schedule requires a sub-classification of long-term loans and advances to assess their quality and recoverability. The specified categories are 'Secured, considered good', 'Unsecured, considered good', and 'Doubtful'. An allowance for bad and doubtful loans and advances must also be disclosed separately under the relevant heads.

May/June 2020

34. 'Long-term Trade Receivables' are classified under which main asset heading in the Balance Sheet?
(A) Current assets
(B) Other non-current assets
(C) Long-term loans and advances
(D) Non-current investments

Ans :

(B) Other non-current assets
While trade receivables are typically current, those with extended credit terms fall under non-current assets. Specifically, 'Long-term Trade Receivables (including trade receivables on deferred credit terms)' are classified as a component of 'Other non-current assets'. This ensures they are not mixed with assets expected to be realized within the operating cycle.

Oct/Nov 2015

35. Which of the following is NOT a classification of 'Inventories' as per Schedule III?
(A) Raw materials
(B) Work-in-progress
(C) Loose tools
(D) Capital work-in-progress

Ans :

(D) Capital work-in-progress
'Capital work-in-progress' is classified under 'Fixed assets' as it relates to the construction of non-current assets. 'Inventories', a current asset, are classified into categories like Raw materials, Work-in-progress, Finished goods, Stock-in-trade, Stores and spares, and Loose tools, all of which relate to the company's ordinary course of business.

May/June 2009

36. A company must separately state the aggregate amount of Trade Receivables outstanding for a period exceeding how many months from their due date?
(A) Three months
(B) Six months
(C) Nine months
(D) Twelve months

Ans :

(B) Six months
To highlight potentially problematic receivables, the schedule mandates a specific disclosure. The aggregate amount of Trade Receivables that are outstanding for a period exceeding six months from the date they are due for payment must be stated separately. This helps stakeholders assess the credit risk and quality of the company's receivables portfolio.

Oct/Nov 2021

37. Which of the following items is NOT classified under 'Cash and cash equivalents'?
(A) Balances with banks
(B) Cheques, drafts on hand
(C) Bank deposits with more than twelve months maturity
(D) Cash on hand

Ans :

(C) Bank deposits with more than twelve months maturity
'Cash and cash equivalents' are highly liquid assets. The schedule specifically requires that 'Bank deposits with more than twelve months maturity' be disclosed separately, implying they are not part of cash equivalents. This category

NODIA

CHAPTER 15

Company Accounts - II

Oct/Nov 2014

1. According to the Companies Act, 2013, which section governs the preparation of a company's final accounts and mandates that they provide a true and fair view of the state of affairs?
   (A) Section 128
   (B) Section 129
   (C) Section 133
   (D) Section 135

   Ans :

   (B) Section 129
   Section 129 of the Companies Act, 2013, specifically governs the preparation of final accounts. It stipulates that the financial statements must present a true and fair view of the company's affairs, comply with accounting standards notified under Section 133, and adhere to the format prescribed in Schedule III for the relevant class of companies.

May/June 2021

2. Under the Companies Act, 2013, which of the following is NOT a mandatory component of a company's financial statements?
   (A) A directors' report on the company's performance
   (B) A balance sheet as at the end of the financial year
   (C) A profit and loss account for the financial year
   (D) A cash flow statement for the financial year

   Ans :

   (A) A directors' report on the company's performance
   As per the definition provided, financial statements in relation to a company include a balance sheet, a profit and loss account, a cash flow statement, a statement of changes in equity (if applicable), and any explanatory notes. The directors' report, while a crucial document, is not listed as a component of the financial statements themselves.

Oct/Nov 2005

3. Which types of companies are specifically exempted from the provisions of Section 129(1) of the Companies Act, 2013, regarding the form of financial statements, if a specific form is prescribed under their governing Act?
   (A) Manufacturing and trading companies
   (B) Information technology and service companies
   (C) Insurance, banking, and electricity generation companies
   (D) Holding and subsidiary companies of foreign entities

   Ans :

   (C) Insurance, banking, and electricity generation companies
   The second proviso to Section 129(1) states that its requirements shall not apply to any insurance company, banking company, or any company engaged in the generation or supply of electricity. This exemption is applicable when a specific form of financial statement is already specified in the Act that governs that particular class of company.

May/June 2010

4. For which of the following company types is the inclusion of a cash flow statement in their financial statements optional?
   (A) Public limited companies
   (B) Private limited companies with turnover above ₹100 crores
   (C) Companies listed on a stock exchange
   (D) One Person Company, small company, and dormant company

   Ans :

   (D) One Person Company, small company, and dormant company
   A proviso within the definition of financial statements under the Companies Act, 2013, specifies an exemption. It states that the financial statement, with respect to a One Person Company, a small company, and a dormant company, may

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(B) Separately disclosing revenue from Sale of products, Sale of services, and Other operating revenues, less Excise duty.

The general instructions for the P&L statement require a detailed breakdown of revenue for a non-finance company. The notes must separately disclose revenue from the sale of products, sale of services, and other operating revenues. From this total, any Excise duty collected is shown as a deduction to arrive at net revenue.

Oct/Nov 2014

43. How must a finance company disclose its 'Revenue from operations'?

(A) As revenue from Sale of products and Sale of services.
(B) As a single consolidated figure titled 'Operating Income'.
(C) It must include revenue from Interest and Other financial services.
(D) It must show Dividend Income and Net gain on sale of investments.

Ans :

(C) It must include revenue from Interest and Other financial services.

The nature of a finance company's business is different, and its revenue recognition reflects this. For a finance company, 'Revenue from operations' is required to include revenue generated from its core activities, which are primarily 'Interest' income and income from 'Other financial services', with each head disclosed separately in the notes.

May/June 2021

44. Which of the following is NOT classified under 'Finance Costs' in the P&L statement?

(A) Interest expense
(B) Dividend Income
(C) Other borrowing costs
(D) Applicable net gain/loss on foreign currency transactions and translation.

Ans :

(B) Dividend Income

'Dividend Income' is a form of income, not a cost. It is classified under 'Other Income'. 'Finance Costs', as per the schedule, relate to the cost of borrowing funds and include items like interest expense, other borrowing costs, and applicable net gains or losses on foreign currency transactions related to borrowings.

Oct/Nov 2005

45. An item of income or expenditure must be disclosed separately as additional information if it exceeds a certain threshold. What is this threshold?

(A) 1 % of the revenue from operations or ₹1,00,000, whichever is higher.
(B) 5 % of the revenue from operations or ₹1,00,000, whichever is higher.
(C) 1 % of the total revenue or ₹10,00,000, whichever is lower.
(D) 2 % of the profit before tax or ₹5,00,000, whichever is higher.

Ans :

(A) 1 % of the revenue from operations or ₹1,00,000, whichever is higher.

To ensure material items of income and expenditure are not hidden within broad categories, a disclosure threshold is set. The company must separately disclose any item of income or expenditure which exceeds one per cent of the revenue from operations or ₹1,00,000, whichever is higher. This ensures significant items are brought to the users' attention.

May/June 2010

46. Which of the following is NOT a required separate disclosure under 'Employee Benefits Expense'?

(A) Salaries and wages
(B) Payments to auditor for taxation matters
(C) Contribution to provident and other funds
(D) Staff welfare expenses

Ans :

(B) Payments to auditor for taxation matters

Payments to the auditor are a separate disclosure item and not part of employee benefits. The schedule requires 'Employee Benefits Expense' to be broken down into specific components, including salaries and wages, contributions to provident and other funds, expenses on ESOP/ ESPP, and general staff welfare expenses.

Oct/Nov 2023

47. What specific information regarding imports must be disclosed by way of a note to the P&L account?

(A) The names of all foreign suppliers.
(B) A comparison of import costs with domestic procurement costs.
(C) The F.O.B. value of all imports during the financial year.

NODIA

Oct/Nov 2007

73. A company's Statement of Profit and Loss shows Revenue from Operations as ₹50 crores and Other Income as ₹2 crores. Its expenses include Cost of Materials Consumed at ₹25 crores, Employee Benefits Expense at ₹10 crores, and Finance Costs at ₹3 crores. It has no other expenses, exceptional items, or tax. What is the 'Profit before exceptional and extraordinary items and tax' for the company?

(A) ₹12 crores
(B) ₹15 crores
(C) ₹14 crores
(D) ₹25 crores

Ans :

(C) ₹14 crores
First, calculate Total Revenue: Revenue from Operations (₹50 cr) + Other Income (₹2 cr) = ₹52 crores. Next, calculate Total Expenses: Cost of Materials (₹25 cr) + Employee Benefits (₹10 cr) + Finance Costs (₹3 cr) = ₹38 crores. Profit before tax is Total Revenue - Total Expenses, which is ₹52 cr - ₹38 cr = ₹14 crores.

May/June 2025

74. ABC Ltd., a manufacturing company, paid its statutory auditor the following amounts during the year: ₹5,00,000 as audit fees, ₹1,00,000 for tax representation services, and ₹50,000 as reimbursement of out-of-pocket expenses. As per the additional information required for the P&L statement, how should the payments to the auditor be disclosed?

(A) A single amount of ₹6,50,000 as 'Auditor's Remuneration'.
(B) Only the audit fee of ₹5,00,000 needs to be disclosed.
(C) A total of ₹6,00,000 as fees and ₹50,000 as expenses.
(D) Disclosed separately as (a) auditor: ₹5,00,000; (b) for taxation matters: ₹1,00,000; and (f) for reimbursement of expenses: ₹50,000.

Ans :

(D) Disclosed separately as (a) auditor: ₹5,00,000; (b) for taxation matters: ₹1,00,000; and (f) for reimbursement of expenses: ₹50,000.
The schedule requires a detailed breakup of payments to the auditor. It specifies separate disclosure for payments as (a) auditor, (b) for taxation matters, (c) for company law matters, (d) for management services, (e) for other services, and (f) for reimbursement of expenses. The scenario requires this specific, disaggregated disclosure.

Oct/Nov 2024

75. A company holds investments in the shares of a subsidiary. At the beginning of the year, the carrying amount was ₹10 crores. During the year, it purchased additional shares for ₹2 crores. At the year-end, the market value is ₹15 crores. The investments are carried at cost. What would the reconciliation of 'Non-current investments' show for this class of asset?

(A) Opening balance ₹10 cr, Closing balance ₹15 cr.
(B) Opening balance ₹10 cr, Additions ₹5 cr, Closing balance ₹15 cr.
(C) Opening balance ₹10 cr, Additions ₹2 cr, Closing balance ₹12 cr.
(D) Opening balance ₹10 cr, Additions ₹2 cr, Revaluation gain ₹3 cr, Closing balance ₹15 cr.

Ans :

(C) Opening balance ₹10 cr, Additions ₹2 cr, Closing balance ₹12 cr.
The reconciliation shows the movement in the carrying amount. Since the investments are carried at cost, the market value is irrelevant for the carrying amount reconciliation (though it might be disclosed separately). The reconciliation would start with the opening balance (₹10 cr), show the additions during the period (₹2 cr), and arrive at the closing balance (₹12 cr).

May/June 2020

76. A company purchased raw materials worth ₹50 lakhs on credit. As per the balance sheet date, ₹10 lakhs is outstanding to the supplier. The company also has an outstanding bank overdraft of ₹25 lakhs. How should the ₹10 lakhs and ₹25 lakhs be classified in the balance sheet?

(A) Both as 'Trade payables'.
(B) ₹10 lakhs as 'Trade payables' and ₹25 lakhs as 'Short-term borrowings'.
(C) Both as 'Other current liabilities'.
(D) ₹10 lakhs as 'Other current liabilities' and ₹25 lakhs as 'Trade payables'.

Ans :

(B) ₹10 lakhs as 'Trade payables' and ₹25 lakhs as 'Short-term borrowings'.

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statements, and this change has a material effect on the opening balance sheet information.

May/June 2019

52. Which of the following items is a line item specifically required to be presented on the face of the Balance Sheet by Ind AS-1?
(A) Capital work-in-progress
(B) Investment property
(C) Short-term borrowings
(D) Trade payables

Ans :

(B) Investment property
Ind AS-1 prescribes certain minimum line items for the balance sheet. Among the options given, 'investment property' is explicitly listed as a line item to be presented. While items like borrowings and payables are also on the balance sheet, 'investment property' is a distinct category specified by the standard for separate presentation.

Oct/Nov 2022

53. How does Ind AS-1 require deferred tax assets and liabilities to be classified in the balance sheet?
(A) Always as current assets and current liabilities.
(B) As current or non-current based on the expected timing of their reversal.
(C) Always as non-current assets and non-current liabilities.
(D) As part of equity under a separate reserve.

Ans :

(C) Always as non-current assets and non-current liabilities.
Ind AS-1 provides a specific rule for deferred tax. When an entity presents current and non-current classifications, it shall not classify deferred tax assets (liabilities) as current assets (liabilities). This means they are always presented under the non-current category, regardless of their expected reversal period, to ensure consistent presentation.

May/June 2013

54. According to Ind AS-1, which of the following is NOT a criterion for classifying an asset as 'current'?
(A) It is expected to be realised within twelve months after the reporting period.
(B) It is held primarily for the purpose of trading.
(C) It is cash or a cash equivalent unless restricted for at least twelve months.
(D) It is an intangible asset with a finite useful life of less than 12 months.

Ans :

(D) It is an intangible asset with a finite useful life of less than 12 months.
The criteria for classifying an asset as current under Ind AS-1 are specific and do not make a special case for intangible assets based on their useful life. The criteria focus on realization within the operating cycle or 12 months, the purpose of holding (trading), or if it is cash or a cash equivalent.

Oct/Nov 2006

55. Under Ind AS-1, how should an entity present its Statement of Profit and Loss?
(A) In a traditional two-column 'T' format, showing all debits on the left and all credits on the right.
(B) As a single statement presenting profit or loss and other comprehensive income in two distinct sections.
(C) The entity has a free choice between a single combined statement or two separate statements for profit or loss and OCI.
(D) As a detailed statement of retained earnings that shows all individual income and expense items for the period.

Ans :

(B) As a single statement presenting profit or loss and other comprehensive income in two distinct sections.
Ind AS-1 mandates a specific structure. An entity should present a single statement of profit and loss, with profit or loss and other comprehensive income (OCI) presented in two distinct sections. The profit or loss section must be presented first, followed directly by the other comprehensive income section, culminating in total comprehensive income.

May/June 2024

56. What is the treatment of 'extraordinary items' under Ind AS-1?
(A) They are presented separately after profit after tax.
(B) They are disclosed in the notes but not on the face of the P&L statement.

NODIA

Oct/Nov 2011

65. An NBFC (a finance company) earns income from interest on loans, fees for loan processing, and profit from the sale of a company car. Based on the source, which of these would be included in its 'Revenue from operations'?

(A) Only interest on loans and fees for loan processing.
(B) Only interest on loans.
(C) Only profit from the sale of the company car.
(D) All three items: interest, processing fees, and profit on car sale.

Ans :

(A) Only interest on loans and fees for loan processing.
The source specifies that for a finance company, revenue from operations includes 'Interest' and 'Other financial services'. Interest on loans clearly falls under the first category. Fees for loan processing are a core operational activity and would be classified under 'Other financial services'. Profit on the sale of a car is non-operating income and would be shown under 'Other Income'.

May/June 2017

66. An investor holds 40 % of the voting rights in Company X and has a contractual right to appoint the majority of the board. The investor is also entitled to performance-based fees. According to the source, does the investor control Company X?

(A) No, because the investor holds less than 51 % of voting rights.
(B) Yes, because it has power, exposure to variable returns, and the ability to use that power.
(C) No, because performance fees are not considered variable returns.
(D) It cannot be determined without knowing the identity of other shareholders.

Ans :

(B) Yes, because it has power, exposure to variable returns, and the ability to use that power.
The source defines control through three concurrent elements. The contractual right to appoint the board gives the investor 'power'. The performance-based fees provide 'exposure to variable returns'. The ability to direct activities via the board to influence those fees demonstrates the 'ability to use power to affect returns'. All three conditions are met.

Oct/Nov 2025

67. A former employee has filed a lawsuit against a company for ₹50 lakhs. The company's legal counsel believes the claim is baseless and the company has not accepted the liability. How should this be treated in the financial statements, according to the source?

(A) It should be ignored as the company has not acknowledged the debt.
(B) It should be recorded as a long-term provision for the full amount.
(C) It should be recorded as a current liability.
(D) It should be disclosed as a contingent liability under 'Claims against the company not acknowledged as debt'.

Ans :

(D) It should be disclosed as a contingent liability under 'Claims against the company not acknowledged as debt'.
The source text clearly outlines the classification for contingent liabilities. A lawsuit that the company is contesting and has not accepted as a valid debt fits perfectly into the category "Claims against the company not acknowledged as debt". It is a potential obligation disclosed in the notes, not a recognized liability or provision.

May/June 2012

68. A company's total trade receivables are ₹2 crores. Out of this, ₹30 lakhs are due for more than six months, and ₹15 lakhs are due for more than twelve months. Based on the provided instruction, what amount must be separately stated?

(A) ₹30 lakhs
(B) ₹15 lakhs
(C) ₹45 lakhs
(D) ₹2 crores

Ans :

(A) ₹30 lakhs
The instruction requires the separate disclosure of the aggregate amount of receivables outstanding for a period exceeding six months from the due date. The ₹15 lakhs (due over 12 months) is a subset of the ₹30 lakhs (due over 6 months). Therefore, the total aggregate amount to be disclosed under this specific note is ₹30 lakhs.

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(A) To reconcile the carrying amount of each component of equity from the beginning to the end of the period.
The Statement of Changes in Equity serves to detail the movement in the owners' stake in the company. It presents a reconciliation for each component of equity (like share capital, retained earnings, and other reserves) between the carrying amount at the start and end of the reporting period, disclosing changes from profit/loss, OCI, and owner transactions.

Oct/Nov 2012

61. A company has a turnover of ₹95 crores for the financial year. According to the provided text, which of the following rounding off conventions is NOT permissible for this company's financial statements?
(A) Rounding off to the nearest thousands.
(B) Rounding off to the nearest lakhs.
(C) Rounding off to the nearest crores.
(D) Rounding off to the nearest millions.

Ans :

(C) Rounding off to the nearest crores.
The source states that for a company with a turnover of less than one hundred crore rupees, figures can be rounded off to the nearest hundreds, thousands, lakhs, or millions. The option to round off to the nearest crores is exclusively available for companies with a turnover of one hundred crore rupees or more.

May/June 2016

62. A company has a bank loan with a final repayment date 18 months from the balance sheet date. However, the loan agreement contains a covenant that, if breached, makes the loan immediately repayable on demand. Based on the source text, how should this loan be classified?
(A) As a non-current liability, because the scheduled final repayment date is beyond 12 months.
(B) As a current liability, because the right to defer settlement is conditional.
(C) As a long-term provision, since the potential repayment is uncertain in its timing.
(D) Split between current and non-current based on a management assessment of the probability of a covenant breach.

Ans :

(B) As a current liability, because the right to defer settlement is conditional.
According to the criteria provided in the source, a liability is current if the company lacks an unconditional right to defer settlement for at least twelve months. The presence of a covenant that could make the loan repayable on demand means the right to defer is conditional, not unconditional, thus mandating a current liability classification.

Oct/Nov 2019

63. Based on the provided classification for 'Reserves and Surplus', which item represents the accumulated profits of the company after all appropriations?
(A) Capital Reserves
(B) Revaluation Reserve
(C) Surplus
(D) Securities Premium Reserve

Ans :

(C) Surplus
The source text explicitly defines 'Surplus' as the "balance in Statement of Profit and Loss disclosing allocations and appropriations such as dividend, bonus shares and transfer to/from reserves". This confirms that 'Surplus' is the specific sub-head within 'Reserves and Surplus' that represents the company's accumulated and retained earnings available for distribution or reinvestment.

May/June 2005

64. A company owns a fleet of trucks used for delivering its products to customers. According to the classification provided in the source text, under which sub-head of Tangible Assets should these trucks be shown?
(A) Plant and Equipment
(B) Others
(C) Vehicles
(D) Office equipment

Ans :

(C) Vehicles
The source provides a clear and specific list for the classification of tangible assets. Item (e) in this list is 'Vehicles'. Therefore, a fleet of trucks used for business operations would be correctly classified under this specific sub-head, distinguishing them from other types of machinery or equipment used by the company.

NODIA

(D) The C.I.F. value of imports of Raw materials, Components/spare parts, and Capital goods.

Ans :

(D) The C.I.F. value of imports of Raw materials, Components/spare parts, and Capital goods.
The profit and loss account must contain a note detailing foreign currency transactions. This includes the value of imports calculated on a C.I.F. (Cost, Insurance, and Freight) basis, with a specific breakdown for raw materials, components and spare parts, and capital goods imported during the financial year.

May/June 2007

48. In the context of Consolidated Financial Statements (CFS), how should 'Minority interests' be presented in the consolidated balance sheet?
(A) As a separate item within equity, but distinct from the equity of the parent's owners.
(B) As a non-current liability.
(C) As a deduction from the consolidated reserves and surplus.
(D) It should be netted against the goodwill on consolidation.

Ans :

(A) As a separate item within equity, but distinct from the equity of the parent's owners.
The general instructions for preparing Consolidated Financial Statements specify the presentation of the non-controlling or minority interest. It states that "Minority interests" in the balance sheet shall be presented within equity, but separately from the equity attributable to the owners of the parent company, reflecting their stake in the subsidiary's net assets.

Oct/Nov 2018

49. Which Indian Accounting Standard (Ind AS) deals primarily with the presentation of financial statements?
(A) Ind AS 110
(B) Ind AS 8
(C) Ind AS 1
(D) Ind AS 7

Ans :

(C) Ind AS 1
Indian Accounting Standard-1 (Ind AS-1) is the cornerstone standard for financial reporting presentation. It is titled "Presentation of Financial Statements" and prescribes the basis for presenting general-purpose financial statements to ensure comparability. It sets out the overall requirements, structure, and minimum content for financial statements.

May/June 2015

50. According to Ind AS-1, which of the following is NOT part of a complete set of financial statements?
(A) A sustainability report for the period
(B) A statement of profit and loss for the period
(C) A statement of changes in equity for the period
(D) A balance sheet as at the end of the period

Ans :

(A) A sustainability report for the period
Ind AS-1 lists the components that constitute a complete set of financial statements. These are the balance sheet, statement of profit and loss, statement of changes in equity, statement of cash flows, notes, and comparative information. A sustainability report, while valuable, is a separate report and not a mandatory component under Ind AS-1.

Oct/Nov 2009

51. Under Ind AS-1, when is an entity required to present a third balance sheet as at the beginning of the preceding period?
(A) Whenever the entity's reported profit or loss for the period increases by more than 25 % compared to the prior year.
(B) When the entity completes a major financing activity, like issuing new shares or debentures, during the current period.
(C) When the entity undergoes a major business combination, such as acquiring a new subsidiary or disposing of a large segment.
(D) When applying an accounting policy retrospectively or making a retrospective restatement of items.

Ans :

(D) When applying an accounting policy retrospectively or making a retrospective restatement of items.
Ind AS-1 mandates the presentation of a third balance sheet (as at the beginning of the preceding period) if an entity applies an accounting policy retrospectively, makes a retrospective restatement of items, or reclassifies items in its financial

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Oct/Nov 2010

69. A company's factory, located in an area not prone to earthquakes, was destroyed by a sudden, unexpected earthquake, resulting in a significant loss. How should this loss be presented in the financial statements prepared under Ind AS, according to the source?

(A) As an extraordinary item, shown separately after profit from continuing operations, net of applicable taxes.
(B) As a non-reclassifiable component of Other Comprehensive Income (OCI) to highlight its unusual nature.
(C) Not as an extraordinary item, but its nature and amount should be disclosed separately as an exceptional item if material.
(D) As a retrospective restatement of the previous year's financial statements to correct the opening position.

Ans :

(C) Not as an extraordinary item, but its nature and amount should be disclosed separately as an exceptional item if material.
The source explicitly prohibits the use of the 'extraordinary item' classification. While the event is unusual and infrequent, under Ind AS, such a material loss would be presented as part of profit or loss from ordinary activities. Its nature and amount would be disclosed separately (often termed 'exceptional') to explain its impact on the company's performance.

May/June 2018

70. A company is engaged in the business of dairy farming. Its primary assets include cows for milk production and land on which the farm is situated. Based on the provided excerpt from Ind AS-1, which of these assets would be presented as 'biological assets'?

(A) The cows used for milk production.
(B) The land on which the farm is situated.
(C) The milk inventory held for sale.
(D) The tractors and farming equipment.

Ans :

(A) The cows used for milk production.
The source mandates the presentation of 'biological assets' as a line item. As defined in Ind AS 41 (referenced in the source), a biological asset is a living animal or plant. Therefore, the cows used for milk production fit this definition. Land is property, milk is inventory (agricultural produce), and tractors are equipment (PPE).

Oct/Nov 2016

71. XYZ Ltd. has a term loan from a bank, with the outstanding amount being ₹5 crores. The loan is repayable in annual instalments of ₹1 crore over the next 5 years. The company is preparing its Balance Sheet as at 31st March 2023. How should XYZ Ltd. classify the ₹5 crore loan in its Balance Sheet as at 31st March 2023?

(A) ₹5 crores as 'Long-term borrowings'.
(B) ₹5 crores as 'Short-term borrowings'.
(C) ₹1 crore as 'Short-term provisions' and ₹4 crores as 'Long-term borrowings'.
(D) ₹1 crore as 'Current maturities of long-term debt' and ₹4 crores as 'Long-term borrowings'.

Ans :

(D) ₹1 crore as 'Current maturities of long-term debt' and ₹4 crores as 'Long-term borrowings'.
The portion of the long-term debt that is due for settlement within twelve months from the reporting date must be classified as a current liability. In this case, the ₹1 crore instalment due within the next year is a 'Current maturity of long-term debt' (under Other Current Liabilities). The remaining ₹4 crores are classified as 'Long-term borrowings'.

May/June 2014

72. A company, PQR Ltd., has an authorized share capital of 1,000,000 equity shares of ₹10 each. It has issued and fully paid up 800,000 shares. During the year, the company forfeited 1,000 shares (on which ₹5 per share was paid) for non-payment of a call of ₹5. In the notes to accounts on Share Capital, what amount should be shown against 'Forfeited shares'?

(A) ₹10,000
(B) ₹5,000
(C) ₹80,05,000
(D) ₹1,000

Ans :

(B) ₹5,000
The disclosure requirement for forfeited shares is the amount originally paid-up on those shares. In this case, 1,000 shares were forfeited, and the amount paid up on them was ₹5 per share. Therefore, the amount to be disclosed under the 'Forfeited shares' line item within the Share Capital note is 1,000 × ₹5 = ₹5,000.

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(C) An entity shall not present any items of income or expense as extraordinary items.
(D) They are presented as a component of other comprehensive income.

Ans :

(C) An entity shall not present any items of income or expense as extraordinary items.
Ind AS-1 explicitly prohibits the presentation of any items of income or expense as 'extraordinary items'. This applies to both the statement of profit and loss and the notes. The concept was removed to improve comparability, with such items now being classified as exceptional and disclosed based on their nature and materiality.

Oct/Nov 2017

57. What is a 'reclassification adjustment' as described in the context of Ind AS-1?
(A) An adjustment to correct a prior period error.
(B) An amount reclassified from profit or loss to other comprehensive income.
(C) An amount previously recognised in other comprehensive income that is reclassified to profit or loss in the current period.
(D) An adjustment made when changing an accounting policy.

Ans :

(C) An amount previously recognised in other comprehensive income that is reclassified to profit or loss in the current period.
A reclassification adjustment refers to amounts that are moved from Other Comprehensive Income (OCI) to the Profit or Loss statement. This typically happens when a gain or loss, previously recognized in OCI as unrealized (e.g., on an available-for-sale financial asset), is realized and needs to be recognized in the current period's profit or loss.

May/June 2008

58. Which of the following items, when recognised in Other Comprehensive Income (OCI), does NOT give rise to a reclassification adjustment in subsequent periods?
(A) Changes in revaluation surplus on property, plant, and equipment under Ind AS 16.
(B) Gains on cash flow hedges.
(C) Gains on financial assets measured at FVTOCI.
(D) Exchange differences on translating foreign operations.

Ans :

(A) Changes in revaluation surplus on property, plant, and equipment under Ind AS 16.
Certain components of OCI are never reclassified to profit or loss. Changes in a revaluation surplus recognized under Ind AS 16 are a prime example. This surplus may be transferred directly to retained earnings when the asset is used or derecognised, but it is not recycled through the profit or loss statement.

Oct/Nov 2020

59. Which method of expense analysis is required to be presented by an entity in its statement of profit or loss or in the notes, as per Ind AS-1?
(A) A classification based on the function of expense method.
(B) A classification based on the nature of expense method.
(C) A classification based on the variability of expense (fixed vs. variable).
(D) A classification based on the controllability of expense.

Ans :

(B) A classification based on the nature of expense method.
Ind AS-1 requires an entity to present an analysis of expenses recognised in profit or loss using a classification based on their nature. The 'nature of expense' method aggregates expenses according to their character (e.g., depreciation, purchases of materials, employee benefits, advertising costs) without reallocating them among functions within the entity.

May/June 2011

60. What is the primary purpose of the 'Statement of Changes in Equity'?
(A) To reconcile the carrying amount of each component of equity from the beginning to the end of the period.
(B) To show the reconciliation of cash and cash equivalents.
(C) To list all transactions with related parties during the period.
(D) To provide a detailed breakdown of revenue from operations.

Ans :

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A 'trade payable' arises from goods purchased or services received in the normal course of business. The ₹10 lakhs due to the supplier fits this definition. A bank overdraft is a form of borrowing, repayable on demand, and is therefore classified under 'Short-term borrowings'.

Oct/Nov 2015

77. A company, DEF Ltd., applies an accounting policy for inventory valuation retrospectively. This change has a material effect on the financial statements. The company is preparing its statements for the year ended 31 March 2024. According to Ind AS-1, what is the minimum number of balance sheets DEF Ltd. must present?

(A) One, for 31 March 2024.
(B) Two, for 31 March 2024 and 31 March 2023.
(C) Four, including one at the date the policy change was decided.
(D) Three, for 31 March 2024, 31 March 2023, and 1 April 2022.

Ans :

(D) Three, for 31 March 2024, 31 March 2023, and 1 April 2022.
Para 40A of Ind AS-1 requires that if an entity applies an accounting policy retrospectively and it has a material effect, it must present a third balance sheet. This would be for the current period-end (31 Mar 2024), the previous period-end (31 Mar 2023), and the beginning of the preceding period (1 Apr 2022).

May/June 2009

78. A company has 'Unpaid matured debentures' of ₹20 lakhs and 'Interest accrued thereon' of ₹1 lakh. It also has declared a dividend of ₹50 lakhs which remains unpaid as of the balance sheet date. Under which Balance Sheet heading would these three items be classified?

(A) All three under 'Other current liabilities'.
(B) All three under 'Short-term provisions'.
(C) Debentures under 'Long-term borrowings' and the other two under 'Other current liabilities'.
(D) Unpaid dividend under 'Provisions' and the other two under 'Other current liabilities'.

Ans :

(A) All three under 'Other current liabilities'.
The schedule provides specific classifications for these items under the head 'Other current liabilities'. This head includes sub-items like 'Unpaid dividends', 'Unpaid matured debentures and interest accrued thereon', and 'Unpaid matured deposits and interest accrued thereon'. All three items represent current obligations of the company.

Oct/Nov 2021

79. A company has a 10-year loan of ₹100 crore. The terms of the loan require the company to maintain a Debt-to-Equity ratio of 2:1. If the ratio is breached, the bank has the right to demand immediate repayment of the entire loan. At the balance sheet date, the company is in compliance with the covenant. Based on the principles of liability classification in Schedule III, how should the ₹100 crore loan be classified?

(A) As a non-current liability, as the company is compliant at the balance sheet date.
(B) As a contingent liability, because the repayment depends on a future event.
(C) As a current liability, because the right to defer is not unconditional.
(D) Split between current and non-current based on the repayment schedule.

Ans :

(C) As a current liability, because the right to defer is not unconditional.
A liability is current if the company does not have an unconditional right to defer settlement for at least twelve months. The existence of the covenant, which gives the bank the right to demand repayment upon a breach, means the company's right to defer is conditional. Therefore, the entire liability is classified as current.

May/June 2023

80. MNO Inc., a US-based company, has an Indian subsidiary, PQR Ltd. MNO Inc. follows a calendar year financial year (ending Dec 31). PQR Ltd. needs to align its financial year for consolidation purposes. What recourse does PQR Ltd. have regarding its financial year?

(A) It can make an application to the Tribunal to allow its financial year to end on 31st December.
(B) It must follow the 31st March year-end, with no exceptions.
(C) It can automatically adopt the 31st December year-end.
(D) It must prepare two sets of financial statements, one for March 31 and one for Dec

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31.

Ans :

(A) It can make an application to the Tribunal to allow its financial year to end on 31st December. The schedule provides a specific recourse for this situation. A company that is a subsidiary of a foreign entity and needs to follow a different financial year for consolidation can make an application to the Tribunal. If satisfied, the Tribunal may allow a different period as its financial year.

Oct/Nov 2008

81. Which of the following pairs is correctly matched based on Schedule III classification?

(A) Intangible assets under development - Current Assets
(B) Share application money pending allotment - Shareholders' Funds
(C) Loose tools - Fixed Assets
(D) Long-term trade receivables - Other non-current assets

Ans :

(D) Long-term trade receivables - Other non-current assets
'Long-term trade receivables' are correctly classified under 'Other non-current assets'. 'Intangible assets under development' are non-current. 'Share application money pending allotment' is a separate head between equity and liabilities. 'Loose tools' are classified under 'Inventories', which is a current asset. Thus, only the pair in the correct option is correct.

May/June 2006

82. Which of the following is an incorrect statement regarding the Balance Sheet as per Schedule III?

(A) The Balance Sheet has a vertical format with 'Equity and Liabilities' followed by 'Assets'.
(B) Deferred tax assets are classified under current assets.
(C) Figures for the previous reporting period are required to be presented for comparison.
(D) Share capital disclosure requires a reconciliation of shares outstanding.

Ans :

(B) Deferred tax assets are classified under current assets.
In the Schedule III balance sheet format, 'Deferred tax assets (net)' are explicitly placed under the main heading 'Non-current assets'. They are not classified as current assets. The other statements regarding the vertical format, comparative figures, and share capital reconciliation are all correct as per the requirements.

Oct/Nov 2013

83. Consider the following statements about disclosures in financial statements:

1. Details of shares held by shareholders with more than 5 % holding must be disclosed.
2. Aggregate number of shares bought back in the last 10 years must be disclosed.
3. Calls unpaid by directors and officers must be shown separately.

Which of the above statements is/are correct?

(A) 1 only
(B) 1 and 3 only
(C) 2 and 3 only
(D) 1, 2, and 3

Ans :

(B) 1 and 3 only
Statement 1 is correct, as disclosure of holdings greater than 5 % is required. Statement 3 is also correct, as calls unpaid by directors and officers need separate disclosure. Statement 2 is incorrect; the look-back period for disclosing share buybacks is five years, not ten years.

May/June 2022

84. A company has the following items:

1. Unpaid Dividends
2. Interest accrued and due on borrowings
3. Current maturities of long-term debt
4. Provision for employee benefits (payable within 6 months)

Which of these would be classified under 'Other current liabilities'?

(A) 1 and 2 only
(B) 3 and 4 only
(C) All of the above
(D) 1, 2, and 3 only

Ans :

(D) 1, 2, and 3 only
'Unpaid dividends', 'Interest accrued and due on borrowings', and 'Current maturities of long-term debt' are all explicitly listed as classifications under the head 'Other current liabilities'. 'Provision for employee benefits' payable within the short term would be classified under 'Short-term provisions', not 'Other current liabilities'.

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Oct/Nov 2014

85. Match List-I (Asset Category) with List-II (Specific Asset).

	List I (Asset Category)		**List II (Specific Asset)**
P.	Intangible Asset	1.	Investment Property
Q.	Non-current Investment	2.	Mining Rights
R.	Inventory	3.	Security Deposits
S.	Long-term loans & advances	4.	Stores and spares

Select the correct code:
(A) P-2, Q-1, R-4, S-3
(B) P-1, Q-2, R-3, S-4
(C) P-2, Q-4, R-1, S-3
(D) P-3, Q-1, R-4, S-2

Ans :

(A) P-2, Q-1, R-4, S-3
P. 'Mining Rights' are an Intangible Asset. Q. 'Investment Property' is a Non-current Investment. R. 'Stores and spares' are a type of Inventory. S. 'Security Deposits' given by the company are classified under Long-term loans and advances. Therefore, the correct matching is P-2, Q-1, R-4, S-3.

May/June 2021

86. **Assertion (A) :** Under Ind AS, a single Statement of Profit and Loss is presented, which includes a section for 'Other Comprehensive Income'.
Reason (R) : Ind AS prohibits the recognition of any income or expense directly in equity.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(C) (A) is true but (R) is false.
Assertion (A) is true; Ind AS-1 prescribes a single statement with two sections: profit or loss and OCI. However, Reason (R) is false. Certain items, such as some transaction costs on issuing equity or changes resulting from transactions with owners, are recognised directly in equity and are not routed through P&L or OCI.

Oct/Nov 2005

87. Identify the correct sequence of items as they appear in the Equity and Liabilities side of the Balance Sheet as per Schedule III.
1. Non-Current Liabilities
2. Shareholders' Funds
3. Current Liabilities
4. Share application money pending allotment
(A) 2, 1, 4, 3
(B) 4, 2, 1, 3
(C) 2, 4, 3, 1
(D) 2, 4, 1, 3

Ans :

(D) 2, 4, 1, 3
The prescribed vertical format of the Balance Sheet under Schedule III follows a specific order on the 'EQUITY AND LIABILITIES' side. The correct sequence is (1) Shareholders' funds, (2) Share application money pending allotment, (3) Non-current liabilities, and (4) Current liabilities. This corresponds to the sequence 2, 4, 1, 3.

May/June 2010

88. Which of the following statements regarding Ind AS-110 'Consolidated Financial Statements' is incorrect?
(A) An investor controls an investee only if it holds more than 50 % of the voting power.
(B) It establishes control as the basis for consolidation.
(C) Control requires power, exposure to variable returns, and the ability to use power to affect those returns.
(D) A parent must prepare consolidated financial statements using uniform accounting policies.

Ans :

(A) An investor controls an investee only if it holds more than 50 % of the voting power.
Ind AS-110 defines control based on the three elements of power, returns, and the link between them. Power can arise from rights other than voting rights, such as contractual arrangements. Therefore, control can exist even with less than 50 % of voting power, making the statement that control requires more than 50% of voting power incorrect.

Oct/Nov 2023

89. Consider the following items:
1. Brands/trademarks

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May/June 2024

98. **Assertion (A) :** A company must disclose the aggregate amount of loans guaranteed by its directors.
Reason (R) : Such guarantees create a potential conflict of interest and represent a form of related party transaction that users of financial statements need to be aware of.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is true; Schedule III explicitly requires disclosure of the aggregate amount of loans guaranteed by directors under the borrowings note. Reason (R) provides the underlying principle for this disclosure requirement. Guarantees by directors are a significant related party disclosure, essential for assessing governance and potential risks, making it the correct explanation.

Oct/Nov 2017

99. A company has partly paid shares in another company, with an uncalled amount of ₹5 per share on 10,000 shares. How is this uncalled amount of ₹50,000 treated in the financial statements?
(A) As a current liability.
(B) As a provision.
(C) Disclosed as a 'Commitment'.
(D) As a deduction from the investment value.

Ans :

(C) Disclosed as a 'Commitment'.
The uncalled amount on partly paid shares represents a commitment to pay in the future if a call is made. It is not a present obligation (liability). Therefore, it is disclosed under the head 'Commitments' in the notes, specifically as 'Uncalled liability on shares and other investments partly paid'.

May/June 2008

100. In the context of Ind AS-1 presentation, which statement is true?
(A) An entity can present its 'Other Comprehensive Income' items either net of tax or before tax with a single aggregate tax amount.
(B) The standard prescribes a rigid, mandatory format for the Balance Sheet.
(C) All reclassification adjustments must be presented on the face of the P&L statement.
(D) Retrospective adjustments for error corrections are treated as changes in equity for the current period.

Ans :

(A) An entity can present its 'Other Comprehensive Income' items either net of tax or before tax with a single aggregate tax amount. Ind AS-1 offers flexibility here. An entity may present OCI items either net of related tax effects or gross (before tax) with one amount shown for the aggregate income tax relating to those items. The standard does not prescribe a rigid balance sheet format, and adjustments for errors are made to the opening balance of retained earnings.

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Oct/Nov 2020

101. Which of the following statements about the preparation of final accounts for a limited company is correct?
(A) It is desirable but not compulsory by law.
(B) Only companies listed on a stock exchange are required to prepare final accounts.
(C) The format of accounts is determined by the board of directors, not by law.
(D) It is compulsory to prepare a profit and loss account and balance sheet every year.

Ans :

(D) It is compulsory to prepare a profit and loss account and balance sheet every year.
Unlike a sole proprietorship or partnership where it is desirable, for a limited company, it is compulsory to prepare the profit and loss account and the balance sheet every year. This is mandated by the Companies Act, 2013, to ensure accountability to shareholders and other stakeholders and to provide a true and fair view.

May/June 2011

102. Consider the following statements about the Schedule III Balance Sheet format:
1. It is a horizontal format with liabilities on the left and assets on the right.
2. It is a vertical format with assets presented before equity and liabilities.
3. It is a vertical format with equity and

Ans :

(C) Revenue from Operations (Finance Co.) : Net gain on sale of investments

For a finance company, 'Revenue from Operations' includes interest and other financial services income. 'Net gain/loss on sale of investments' is explicitly classified under 'Other income' for all companies, including finance companies, as it is not typically part of the main revenue-generating operations like lending or providing financial services.

May/June 2019

94. A company receives an advance of ₹5 lakhs from a customer for goods to be delivered in the next financial year. How should this amount be classified in the current year's Balance Sheet?

(A) As 'Revenue from operations'.
(B) As 'Other income'.
(C) As a 'Short-term provision'.
(D) As 'Other current liabilities' under the sub-head 'Income received in advance'.

Ans :

(D) As 'Other current liabilities' under the sub-head 'Income received in advance'.

Since the revenue has not yet been earned (as goods are not delivered), the amount received is a liability. It represents an obligation to supply goods or refund the money. The schedule classifies this specifically under 'Other current liabilities' with the sub-head 'Income received in advance'.

Oct/Nov 2022

95. What information does the 'Statement of Changes in Equity' provide that is not readily available from the Balance Sheet and P&L Statement alone?

(A) The detailed reconciliation of movements in each component of equity during the period.
(B) The total assets and liabilities of the company.
(C) The company's earnings per share.
(D) The breakdown of operational expenses by nature.

Ans :

(A) The detailed reconciliation of movements in each component of equity during the period.

While the Balance Sheet shows the closing equity balances and the P&L shows the profit/loss for the period, the Statement of Changes in Equity provides a comprehensive reconciliation. It details how each component of equity (e.g., share capital, retained earnings, revaluation surplus) has moved from the opening to the closing balance.

May/June 2013

96. Which statement accurately reflects the disclosure requirements for 'commitments'?

(A) All commitments must be provided for as liabilities.
(B) Commitments are disclosed under 'Contingent liabilities and commitments'.
(C) Only commitments exceeding 10 % of total assets need to be disclosed.
(D) Commitments are shown as a deduction from fixed assets.

Ans :

(B) Commitments are disclosed under 'Contingent liabilities and commitments'.

Commitments represent future obligations that the company has entered into, such as contracts for capital expenditure. They are not yet liabilities. The schedule requires these to be disclosed (not provided for) in the notes to the financial statements under the heading 'Contingent liabilities and commitments'.

Oct/Nov 2006

97. According to Ind AS-1, notes to financial statements are presented in a specific order to assist users. What is the typical starting point in the notes?

(A) Supporting information for items in the balance sheet.
(B) A statement of compliance with Ind ASs.
(C) Details of contingent liabilities.
(D) The company's financial risk management objectives.

Ans :

(B) A statement of compliance with Ind ASs.

Ind AS-1 suggests a systematic order for presenting notes. The normal order begins with a 'statement of compliance with Ind ASs', followed by a summary of 'significant accounting policies applied', and then the supporting information for line items in the primary statements. This provides a foundational context for the user.

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Oct/Nov 2007

115. Which of the following is the best example of 'Capital work-in-progress'?
(A) A new office building that is under construction.
(B) Raw materials that have been partially processed.
(C) Finished goods that are yet to be sold.
(D) Software that has been purchased and is in use.

Ans :

(A) A new office building that is under construction.
'Capital work-in-progress' represents the cost incurred on fixed assets that are not yet complete or ready for their intended use. A new building under construction is a perfect example. Partially processed raw materials are 'Work-in-progress' (inventory), and software in use is an 'Intangible asset'.

May/June 2025

116. A company receives share application money for an IPO. The issue is oversubscribed. The excess money is refundable to applicants. Where is this refundable amount shown?
(A) Under 'Share application money pending allotment'.
(B) Separately under 'Other current liabilities'.
(C) As a deduction from Share Capital.
(D) As a contingent liability.

Ans :

(B) Separately under 'Other current liabilities'.
The rules for share application money are specific. The portion that is pending allotment (not exceeding issued capital) is shown under its own head. However, any amount that is refundable, such as in the case of oversubscription, must be separately shown under 'Other current liabilities' as it represents a current obligation to pay back the applicants.

Oct/Nov 2024

117. Which of the following is NOT a component of 'Other income' in the P&L statement?
(A) Interest Income (for a non-finance company)
(B) Dividend Income
(C) Other operating revenues
(D) Net gain on sale of investments

Ans :

(C) Other operating revenues
'Other operating revenues' are, by definition, part of the main operations of the business and are included in the calculation of 'Revenue from operations'. 'Other income' comprises non-operating income, which explicitly includes items like interest income (for a non-finance co.), dividend income, and net gain on the sale of investments.

May/June 2020

118. Under Ind AS, changes in revaluation surplus on PPE and re-measurements of defined benefit plans are both:
(A) Recognised in the profit or loss statement.
(B) Recognised in Other Comprehensive Income and later reclassified to profit or loss.
(C) Recognised in Other Comprehensive Income and not reclassified to profit or loss.
(D) Recognised directly in retained earnings, bypassing P&L and OCI.

Ans :

(C) Recognised in Other Comprehensive Income and not reclassified to profit or loss.
Certain components are recognized in OCI and are not subsequently reclassified to profit or loss. Reclassification adjustments do not arise on changes in revaluation surplus (Ind AS 16) or on re-measurements of defined benefit plans (Ind AS 19), as these are not recycled through profit or loss.

Oct/Nov 2015

119. When an entity changes the presentation or classification of items in its financial statements under Ind AS, what must it do with the comparative amounts?
(A) It must remove the comparative amounts for that year.
(B) It must reclassify the comparative amounts unless it is impracticable to do so.
(C) It must only add a note explaining the change without altering the comparative figures.
(D) It must get the change approved by the regulatory authorities.

Ans :

(B) It must reclassify the comparative amounts unless it is impracticable to do so.
To maintain comparability, Para 41 of Ind AS-1 states that if an entity changes the presentation or classification of items, it shall reclassify the

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liabilities presented before assets.

Which of the above statement(s) is/are correct?

(A) 1 only
(B) 2 only
(C) 3 only
(D) 1 and 2 only

Ans :

(C) 3 only

Part I of Schedule III prescribes a vertical format for the Balance Sheet. In this format, the first major section is 'I. EQUITY AND LIABILITIES', which is followed by the second major section, 'II. ASSETS'. Therefore, statement 3 accurately describes the prescribed structure, while statements 1 and 2 are incorrect.

Oct/Nov 2012

103. 'Repairs to machinery' and 'Consumption of stores and spare parts' are required to be disclosed separately as part of what information?

(A) As part of Finance Costs.
(B) As part of Employee Benefits Expense.
(C) As part of the additional information detailing aggregate expenditure on specific items.
(D) As part of the classification of Tangible Assets.

Ans :

(C) As part of the additional information detailing aggregate expenditure on specific items.

The general instructions for the P&L statement require disclosure of additional information. This includes providing a separate figure for the expenditure incurred on specific items, such as 'Consumption of stores and spare parts', 'Power and fuel', 'Rent', 'Repairs to buildings', and 'Repairs to machinery', to provide greater insight into the company's cost structure.

May/June 2016

104. A company reissues debentures that it had previously redeemed. The power to reissue these debentures was available to the company. What is the disclosure requirement for this?

(A) The reissued amount must be shown as 'Other Income'.
(B) No specific disclosure is needed as it is a normal financing activity.
(C) The reissued debentures must be classified as short-term borrowings.
(D) Particulars of any redeemed debentures which the company has power to reissue shall be disclosed.

Ans :

(D) Particulars of any redeemed debentures which the company has power to reissue shall be disclosed.

Under the notes for 'Long-Term Borrowings', there is a specific requirement related to reissuable debentures. The schedule states that particulars of any redeemed bonds/debentures which the company has the power to reissue shall be disclosed. This provides transparency about the company's potential to increase its borrowings without a new authorization process.

Oct/Nov 2019

105. Match List-I (P&L Item) with List-II (Classification).

	List I (P&L Item)		**List II (Classification)**
P.	Interest on bank overdraft	1.	Other Income
Q.	Dividend received from a subsidiary	2.	Employee Benefits Expense
R.	Salaries and Wages	3.	Finance Costs
S.	Loss on sale of fixed asset	4.	Other Expenses

Select the correct code:

(A) P-3, Q-1, R-2, S-4
(B) P-1, Q-2, R-3, S-4
(C) P-3, Q-4, R-2, S-1
(D) P-4, Q-1, R-2, S-3

Ans :

(A) P-3, Q-1, R-2, S-4

P. Interest on a bank overdraft is a borrowing cost, classified under 'Finance Costs'. Q. Dividend received is non-operating income, classified under 'Other Income'. R. 'Salaries and Wages' are a core part of 'Employee Benefits Expense'. S. Loss on sale of a fixed asset is a non-operating expense typically included under 'Other Expenses'.

May/June 2005

106. What is the key objective of presenting comparative information in financial statements?

(A) To increase the length and detail of the annual report.
(B) To allow users to identify trends in the entity's financial position and performance.

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(C) To comply with international tax regulations.
(D) To provide a basis for calculating employee bonuses.

Ans :

(B) To allow users to identify trends in the entity's financial position and performance.
Presenting figures for the preceding period alongside the current period's figures is fundamental for analysis. This comparative information allows users of the financial statements, such as investors and creditors, to assess the company's performance over time and identify significant trends, improvements, or deteriorations in its financial health and operational results.

Oct/Nov 2011

107. If the Board of Directors is of the opinion that a current asset (other than a fixed asset or non-current investment) will not realize its stated value in the ordinary course of business, what action is required?
(A) The asset must be immediately written off to the P&L statement.
(B) The asset's value must be revalued upwards to match its realizable value.
(C) No action is required until the asset is actually sold at a loss.
(D) The fact that the Board is of that opinion shall be stated by way of a note.

Ans :

(D) The fact that the Board is of that opinion shall be stated by way of a note.
This is a specific disclosure requirement to ensure prudence and fair representation. If the Board believes that an asset's carrying amount is higher than its likely realizable value in the ordinary course of business, this opinion must be disclosed in the notes to the financial statements.

May/June 2017

108. A holding company is required to prepare Consolidated Financial Statements (CFS). How should profit or loss attributable to "minority interest" be presented?
(A) It should be presented as an allocation of the total profit or loss for the period.
(B) It should be shown as an expense in the consolidated statement of profit and loss.
(C) It should be adjusted directly against the opening retained earnings.
(D) It is not shown separately in the consolidated financial statements.

Ans :

(A) It should be presented as an allocation of the total profit or loss for the period.
When preparing a consolidated P&L statement, the total profit or loss for the period is calculated for the group as a whole. This total profit is then allocated between the "owners of the parent" and the "minority interest" (or non-controlling interest), and this allocation must be presented in the statement.

Oct/Nov 2025

109. Which of the following is a key component of the 'Statement of Changes in Equity' as prescribed by Ind AS-1?
(A) A reconciliation of property, plant, and equipment.
(B) A list of all cash transactions during the period.
(C) Total comprehensive income for the period, showing amounts attributable to owners and non-controlling interests.
(D) A detailed schedule of short-term and long-term borrowings.

Ans :

(C) Total comprehensive income for the period, showing amounts attributable to owners and non-controlling interests.
A primary requirement for the Statement of Changes in Equity is to present the total comprehensive income for the period. Crucially, it must also show the separate allocation of this total comprehensive income between the amounts attributable to the owners of the parent and the amounts attributable to non-controlling interests.

May/June 2012

110. According to the guidelines for the Balance Sheet under Ind AS-1, how should an entity disclose information about its share capital?
(A) A reconciliation of the number of shares outstanding at the beginning and end of the period.
(B) Only the total value of issued share capital needs to be shown.
(C) The names of all shareholders holding more than 1 % of the shares.
(D) A projection of future share price movements.

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Ans :

(A) A reconciliation of the number of shares outstanding at the beginning and end of the period.

Ind AS-1 requires detailed disclosures for each class of share capital. This includes the number of shares authorised, issued, and paid-up, but very importantly, it also requires a reconciliation of the number of shares outstanding from the beginning to the end of the period, explaining the changes (e.g., new issues, buy-backs).

Oct/Nov 2010

111. A company shows 'Capital Redemption Reserve' in its Balance Sheet. This reserve is created in which of the following situations?

(A) When assets are revalued upwards.
(B) When shares are forfeited for non-payment of calls.
(C) When debentures are redeemed at a premium.
(D) When a company purchases its own shares (buy-back) out of free reserves.

Ans :

(D) When a company purchases its own shares (buy-back) out of free reserves.

While the text lists Capital Redemption Reserve (CRR) as a component of 'Reserves and Surplus', its creation is governed by the Companies Act. CRR is created when a company buys back its own shares using its free reserves or securities premium account, to maintain the capital base.

May/June 2018

112. Which statement is true regarding the classification of 'Current investments'?

(A) They are classified under 'Non-current assets' as they are held for long-term appreciation.
(B) They are expected to be realised within the company's normal operating cycle or twelve months.
(C) The classification includes items like Land and Buildings held for resale.
(D) All current investments must be carried at historical cost.

Ans :

(B) They are expected to be realised within the company's normal operating cycle or twelve months.

'Current investments' are, by definition, a current asset. They are classified as current because they are held with the intention to be sold or realised within the company's normal operating cycle or within twelve months from the reporting date, fitting the general criteria for a current asset.

Oct/Nov 2016

113. What is the purpose of disclosing 'Earmarked balances with banks' separately?

(A) To show the total amount of cash held by the company.
(B) To comply with foreign exchange regulations.
(C) To indicate that these balances are not freely available for general use by the company.
(D) To highlight the amount of interest earned on bank balances.

Ans :

(C) To indicate that these balances are not freely available for general use by the company.

Earmarked balances, such as those held for unpaid dividends or as margin money against guarantees, are restricted in their use. Disclosing them separately from other cash and bank balances is crucial for transparency, as it informs users that these funds are not available for the company's general operational or liquidity needs.

May/June 2014

114. Consider the following liabilities:

1. Trade Payables
2. Long-term Borrowings
3. Short-term Provisions
4. Deferred Tax Liabilities (Net)

Which of these are classified as 'Non-current liabilities' in the Schedule III Balance Sheet?

(A) 1 and 3
(B) 2 and 3
(C) 1 and 4
(D) 2 and 4

Ans :

(D) 2 and 4

In the Schedule III format, 'Long-term Borrowings' and 'Deferred tax liabilities (Net)' are explicitly listed as sub-heads under the major heading 'Non-current liabilities'. 'Trade Payables' and 'Short-term Provisions' are classified under 'Current liabilities', as they are expected to be settled in the near term.

2. Computer software
3. Recipes, formulae, models
4. Investment property

Which of the above are classified as 'Intangible assets' under Schedule III?

(A) 1 and 2 only
(B) 1, 2, and 4
(C) 1, 2, and 3
(D) All of the above

Ans :

(C) 1, 2, and 3

The classification for 'Intangible assets' explicitly includes 'Brands/trademarks', 'Computer software', and 'Recipes, formulae, models, designs and prototypes'. 'Investment property' is a distinct category under 'Non-current investments' (or a separate line item under Ind AS) and is not an intangible asset.

May/June 2007

90. Which of the following is NOT a required disclosure in the notes to the P&L statement regarding foreign currency transactions?

(A) A forecast of future foreign exchange earnings.
(B) C.I.F value of imports of capital goods.
(C) Expenditure in foreign currency on account of royalty and know-how.
(D) Total value of all imported and indigenous raw materials consumed and the percentage of each to total consumption.

Ans :

(A) A forecast of future foreign exchange earnings.

The disclosure requirements focus on historical data. They mandate disclosure of the C.I.F. value of imports, foreign currency expenditure on specific items like royalty, and a comparison of imported vs. indigenous consumption. A forecast of future earnings is a forward-looking statement and is not a required disclosure in the notes.

Oct/Nov 2018

91. What is the primary difference in the treatment of 'Extraordinary Items' between Schedule III (Companies Act, 2013) and Ind AS-1?

(A) Schedule III requires them to be shown before tax, while Ind AS-1 requires them post-tax.
(B) Schedule III classifies them under OCI, while Ind AS-1 includes them in P&L.
(C) There is no difference; both standards treat them identically.
(D) Schedule III allows their presentation on the P&L face, while Ind AS-1 prohibits their classification altogether.

Ans :

(D) Schedule III allows their presentation on the P&L face, while Ind AS-1 prohibits their classification altogether.

The format of the P&L statement in Schedule III includes a specific line item for 'Extraordinary Items'. In contrast, Ind AS-1 explicitly states that an entity shall not present any items of income or expense as extraordinary items, either in the statement of profit and loss or in the notes.

May/June 2015

92. Which of the following is the most appropriate description of 'Other Comprehensive Income' (OCI)?

(A) Income and expenses that are not part of the company's main operations.
(B) Specific income and expense items that are required by other Ind AS to be recognised outside of profit or loss.
(C) All non-cash income and expenses, such as depreciation.
(D) Items of income and expense related to prior periods.

Ans :

(B) Specific income and expense items that are required by other Ind AS to be recognised outside of profit or loss.

Other Comprehensive Income comprises items of income and expense (including reclassification adjustments) that are not recognised in profit or loss as required or permitted by other Indian Accounting Standards. Examples include changes in revaluation surplus and gains/losses on certain financial instruments, which are held directly in equity reserves.

Oct/Nov 2009

93. Identify the incorrect pair.

(A) Finance Costs : Interest expense
(B) Other Income : Dividend Income
(C) Revenue from Operations (Finance Co.) : Net gain on sale of investments
(D) Employee Benefits Expense : Staff welfare expenses

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comparative amounts to conform with the new presentation. This is mandatory unless doing so is impracticable, in which case specific disclosures about the impracticability are required.

May/June 2009

120. What is the fundamental principle for consolidation of a subsidiary under Ind AS-110?
(A) The parent controls the investee.
(B) The parent holds a majority of the equity shares.
(C) The parent has the ability to appoint the majority of the directors.
(D) The parent and subsidiary are in the same line of business.

Ans :

(A) The parent controls the investee.
Ind AS-110 establishes a single, definitive basis for consolidation: control. An investor (parent) must consolidate an investee (subsidiary) if it controls the investee. The standard then provides a detailed definition of control, moving beyond simple majority ownership to a more substance-over-form approach based on power, returns, and the link between them.

Oct/Nov 2021

121. Which of the following is NOT a circumstance that would give rise to separate disclosure of an item of income or expense under Ind AS-1?
(A) Write-downs of inventories to net realisable value.
(B) Disposals of items of property, plant, and equipment.
(C) Litigation settlements.
(D) Routine advertising costs incurred during the period.

Ans :

(D) Routine advertising costs incurred during the period.
Ind AS-1 lists several circumstances that would lead to separate disclosure of material income/expense items due to their nature. These include write-downs, restructurings, disposals, and litigation settlements. Routine operational expenses like advertising costs, unless exceptionally large or unusual, are typically aggregated under the 'nature of expense' classification without separate disclosure.

May/June 2023

122. A company has bank balances of ₹50 lakhs, cheques on hand of ₹5 lakhs, and a 2-year fixed deposit of ₹20 lakhs. What is the amount of 'Cash and cash equivalents'?
(A) ₹75 lakhs
(B) ₹55 lakhs
(C) ₹50 lakhs
(D) ₹25 lakhs

Ans :

(B) ₹55 lakhs
'Cash and cash equivalents' include highly liquid assets. This would encompass the balances with banks (₹50 lakhs) and the cheques on hand (₹5 lakhs). The 2-year fixed deposit has a maturity of more than twelve months and must be disclosed separately, so it is excluded from cash and cash equivalents. Total is ₹50 + ₹5 = ₹55 lakhs.

Oct/Nov 2008

123. The term 'mutatis mutandis' is used in the context of preparing Consolidated Financial Statements. What does it imply?
(A) That a completely different set of rules applies to CFS.
(B) That the preparation of CFS is optional for all companies.
(C) That the requirements of the Schedule apply to CFS with the necessary changes being made.
(D) That only the asset side of the balance sheet needs to be consolidated.

Ans :

(C) That the requirements of the Schedule apply to CFS with the necessary changes being made.
'Mutatis mutandis' is a Latin phrase meaning "with the necessary changes having been made". In this context, it means that the rules and formats specified in Schedule III for a standalone company's financial statements should also be followed for preparing consolidated financial statements, adapting them as necessary for the consolidation context.

May/June 2006

124. Consider the following statements about Ind AS-1:
1. An entity must present a 'Statement of Changes in Assets' for the period.
2. An entity must disclose the measurement basis used in preparing the financial

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statements.
3. An entity must present a balance sheet at the beginning of the preceding period if it applies a policy retrospectively.

Which of the statements are correct?
(A) 1 and 2 only
(B) 1 and 3 only
(C) 1, 2 and 3
(D) 2 and 3 only

Ans :

(D) 2 and 3 only
Statement 1 is incorrect; Ind AS-1 requires a 'Statement of Changes in Equity', not assets. Statement 2 is correct, as disclosing the measurement basis (e.g., historical cost, fair value) is a key part of the accounting policies note. Statement 3 is also correct, as a third balance sheet is required for material retrospective changes.

Oct/Nov 2013

125. Match List-I (Schedule III Item) with List-II (Main Heading).

List I (Schedule III Item)		**List II (Main Heading)**	
P.	Goodwill	1.	Current assets
Q.	Trade receivables	2.	Non-current assets
R.	Money received against Share Warrants	3.	Current liabilities
S.	Trade payables	4.	Shareholders' funds

Select the correct code:
(A) P-2, Q-1, R-4, S-3
(B) P-1, Q-2, R-3, S-4
(C) P-2, Q-4, R-1, S-3
(D) P-4, Q-1, R-2, S-3

Ans :

(A) P-2, Q-1, R-4, S-3
P. Goodwill is a non-current asset. Q. Trade receivables are a current asset. R. Money received against Share Warrants is part of Shareholders' funds. S. Trade payables are a current liability. Therefore, the correct matching is P-2, Q-1, R-4, S-3.

May/June 2022

126. Which of the following disclosures is NOT required under the 'Long-Term Borrowings' note?
(A) Sub-classification as secured and unsecured.
(B) The credit rating assigned to the company.
(C) Terms of repayment of term loans.
(D) Period and amount of continuing default in repayment of loans and interest.

Ans :

(B) The credit rating assigned to the company.
The notes for long-term borrowings require extensive disclosures, including security details, repayment terms, and information on any defaults. However, the text provided does not mandate the disclosure of the company's credit rating as part of this specific note, although it may be disclosed elsewhere in the annual report.

Oct/Nov 2014

127. **Assertion (A) :** The definition of 'control' under Ind AS-110 is complex and requires judgment.
Reason (R) : Power over an investee can arise from various rights, not just voting rights, and may result from one or more contractual arrangements.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is true; assessing control is not always straightforward. Reason (R) correctly explains why this is the case. Because power can stem from complex contractual arrangements beyond simple shareholding, assessing who has the current ability to direct relevant activities requires significant judgment, making the reason a direct explanation for the assertion.

May/June 2021

128. An entity presents its expenses by function (e.g., cost of sales, administrative expenses). What additional disclosure does Ind AS-1 require from such an entity?
(A) A forecast of expenses for the next period.
(B) A reconciliation of expenses with cash paid.
(C) Additional disclosure on the nature of expenses, including depreciation and employee benefit expense.
(D) No additional disclosure is required if the

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function of expense method is used.

Ans :

(C) Additional disclosure on the nature of expenses, including depreciation and employee benefit expense.
While Ind AS-1 allows presentation by function, the 'nature of expense' method is considered simpler. Standard practice under Ind AS-1 is that if an entity uses the function method, it must provide additional disclosures in the notes about the nature of expenses (e.g., depreciation, amortization, employee benefits).

Oct/Nov 2005

129. The 'Let Us Sum Up' section highlights a key point regarding statutory requirements. What is it?

(A) The underlying accounting theory for a limited company is identical to that for a sole proprietorship.
(B) The vertical format of financial statements is universally considered easier to prepare than the horizontal T-account format.
(C) Careful attention to statutory notes and disclosure instructions is required.
(D) Indian Accounting Standards (Ind AS) have been made mandatory for all public and private companies in India.

Ans :

(C) Careful attention to statutory notes and disclosure instructions is required.
The summary emphasizes that while accounting principles might be similar, the crucial aspect of company accounts is the compulsory adherence to prescribed forms and disclosures. It specifically states, "Special care is required to be taken so far as the notes and instructions regarding statutory requirements in respect of the various items are to be disclosed."

May/June 2010

130. Which of the following is NOT listed as a keyword at the end of the chapter?

(A) Earnings Per Share
(B) Final Accounts
(C) Vertical Form
(D) Horizontal Form

Ans :

(A) Earnings Per Share

The 'KEYWORDS' section at the end of the chapter lists the following terms: "Final Accounts; Profit and Loss Appropriation Account; Horizontal Form; Vertical Form; Contingent Liabilities". 'Earnings Per Share', while an important metric shown on the P&L statement, is not included in this specific list of keywords.

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(D) The principal is financing, and the interest may be classified as an operating activity.

The repayment of the principal amount of a loan reduces borrowings, which is a financing activity. The interest element, however, is a cost of finance that is often linked to the entity's profitability and operations. Therefore, Ind AS-7 allows for the interest component to be classified under operating activities while the principal component is classified under financing activities.

May/June 2023

38. Why is the amount of cash flows arising from operating activities considered a key indicator for an entity?

(A) It indicates the entity's ability to repay loans, pay dividends, and make new investments without external financing.

(B) It reveals the degree to which the entity depends on issuing new equity shares for funding.

(C) It serves as the main indicator of success for the entity's long-term investment portfolio and strategy.

(D) It functions as the single and most important determinant of the company's market stock price.

Ans :

(A) It indicates the entity's ability to repay loans, pay dividends, and make new investments without external financing.

Strong positive cash flow from operations is a sign of a healthy, self-sustaining business. It demonstrates that the core business activities are generating enough cash to cover obligations like loan repayments, maintain operating capability, reward shareholders with dividends, and fund new investments, all without needing to raise additional debt or equity from external sources.

Oct/Nov 2024

39. What is the primary reason for the separate disclosure of cash flows from investing activities?

(A) To help predict future claims on cash flows made by the company's providers of debt and equity capital.

(B) To report the total amount of cash that was spent on daily, routine business operating activities.

(C) To represent the extent of expenditures made for resources intended to generate future income and cash flows.

(D) To disclose the aggregate amount of interest and dividends that were paid out during the reporting period.

Ans :

(C) To represent the extent of expenditures made for resources intended to generate future income and cash flows.

Investing activities involve the acquisition and disposal of long-term assets. Disclosing these cash flows separately is important because they highlight the company's strategy for future growth. These expenditures are investments in resources, like new machinery or technology, that are expected to produce income and positive cash flows in the long run.

May/June 2018

40. The separate disclosure of cash flows from financing activities is useful for predicting what?

(A) Claims on future cash flows by the entity's providers of capital

(B) The company's future sales revenue

(C) The efficiency of the company's inventory management

(D) The amount of depreciation to be charged in the next period

Ans :

(A) Claims on future cash flows by the entity's providers of capital

Financing activities involve transactions with owners (equity) and lenders (debt). By analyzing these cash flows, users can understand how the entity is funded and predict future obligations to these capital providers. For example, a large inflow from new debt suggests future cash outflows for interest and principal repayments, which are claims on future cash flows.

Oct/Nov 2025

41. How should cash flows arising from a transaction in a foreign currency be recorded in an entity's functional currency?

(A) By translating the amount using the closing exchange rate effective on the final day of the financial year.

(B) By applying a weighted average exchange rate calculated for the entire duration of the reporting period.

(C) By converting the flow using the specific exchange rate that was in effect at the start of

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for both the Profit & Loss account and the Balance Sheet in statutory annual reports.

(C) To accurately compute the final tax liability that the company owes to tax authorities for a specific accounting period.

(D) To provide users a basis to assess the enterprise's ability to generate cash and cash equivalents.

Ans :

(D) To provide users a basis to assess the enterprise's ability to generate cash and cash equivalents.

The main utility of a cash flow statement is to offer stakeholders, such as investors and creditors, a clear view of an enterprise's capacity to generate cash and cash equivalents. This information is crucial for evaluating the entity's liquidity, solvency, and overall financial health, providing insights beyond what the income statement or balance sheet alone can offer.

Oct/Nov 2023

5. A simple trading enterprise starts its business on 1/04/2022 with ₹1,00,000 in Capital and ₹1,00,000 in Cash. On 2/04/2022, it buys wheat for ₹90,000 and sells it for ₹95,000 on a cash basis. What is the cash balance at the end of 2/04/2022?

(A) ₹95,000
(B) ₹1,00,000
(C) ₹1,05,000
(D) ₹1,95,000

Ans :

(C) ₹1,05,000

The initial cash balance was ₹1,00,000. A cash outflow of ₹90,000 occurred for the purchase of wheat, and a cash inflow of ₹95,000 occurred from its sale. The net change in cash is an inflow of ₹5,000 (₹ 95,000 - ₹ 90,000). Therefore, the closing cash balance is the opening balance plus the net inflow: ₹ 1,00,000 + ₹ 5,000 = ₹ 1,05,000.

May/June 2008

6. The trading activity on 2/04/2022, where a firm buys and sells goods, resulting in a cash inflow of ₹5,000, is classified under which category in a cash flow statement?

(A) Investing activity
(B) Operating activity
(C) Financing activity
(D) Non-cash activity

Ans :

(B) Operating activity

The purchase and sale of goods are principal revenue-producing activities of a trading firm. Therefore, the cash flows resulting from these transactions are classified as operating activities. In this case, the net cash inflow of ₹5,000 from trading is a direct result of the core business operations and is categorized accordingly in accounting parlance.

Oct/Nov 2012

7. Based on a scenario where a firm buys wheat for ₹80,000, sells it for ₹85,000 cash, and buys a machine for ₹15,000 on 3/04/2022, what is the net cash flow from operating activities on that day?

(A) A net cash outflow of ₹10,000
(B) A net cash inflow of ₹85,000
(C) A net cash outflow of ₹80,000
(D) A net cash inflow of ₹5,000

Ans :

(D) A net cash inflow of ₹5,000

Operating activities on this day consist of the purchase and sale of wheat. The cash inflow from the sale is ₹85,000, and the cash outflow for the purchase is ₹80,000. The net cash flow from operating activities is the difference between these two amounts, which is a net inflow of ₹5,000 (₹ 85,000 - ₹ 80,000).

May/June 2017

8. In a scenario where a firm purchases a weighing machine for ₹15,000 on 3/04/2022, this transaction is an example of which type of activity?

(A) Investing activity
(B) Operating activity
(C) Financing activity
(D) Miscellaneous expense activity

Ans :

(A) Investing activity

The weighing machine is a fixed asset acquired to facilitate operations. The acquisition of long-term assets, such as plant and equipment, is classified as an investing activity. This cash outflow of ₹15,000 is not part of the principal revenue-producing activities but rather an investment intended to support future business operations and generate income.

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Oct/Nov 2021

9. Considering a net operating inflow of ₹5,000 and an investing outflow for a machine of ₹15,000 on 3/04/2022, what is the total net cash flow for the day?
(A) A net cash inflow of ₹5,000
(B) A net cash outflow of ₹15,000
(C) A net cash outflow of ₹10,000
(D) A net cash inflow of ₹20,000

Ans :

(C) A net cash outflow of ₹10,000
On 3/04/2022, there was a net cash inflow of ₹5,000 from operating activities (sale of wheat less purchase of wheat). There was also a cash outflow of ₹15,000 for an investing activity (purchase of a machine). The total net cash flow for the day is the sum of these, resulting in a net outflow of ₹10,000.

May/June 2011

10. If a firm's cash balance at the start of 3/04/2022 was ₹1,05,000 and it had a total net cash outflow of ₹10,000 for the day, what would be the firm's cash balance at the end of the day?
(A) ₹95,000
(B) ₹1,15,000
(C) ₹1,05,000
(D) ₹85,000

Ans :

(A) ₹95,000
The cash balance at the beginning of 3/04/2022 was ₹1,05,000. The day's transactions resulted in a total net cash outflow of ₹10,000 (a ₹5,000 inflow from operations and a ₹15,000 outflow from investing). Therefore, the closing cash balance is the opening balance minus the net outflow: ₹ 1,05,000 - ₹ 10,000 = ₹ 95,000.

Oct/Nov 2007

11. If a firm's P&L account had a balance of ₹5,000 at the start of 3/04/2022, and on that day it generated a profit of ₹5,000 from trading, what is the value of the P&L account at the end of the day?
(A) ₹5,000
(B) ₹15,000
(C) ₹20,000
(D) ₹10,000

Ans :

(D) ₹10,000
The P&L account balance at the start of the day was ₹5,000. The trading activity on 3/04/2022 (selling wheat for ₹85,000 that was bought for ₹80,000) generated an additional profit of ₹5,000. This profit is added to the P&L account, bringing the new balance to ₹10,000 (₹ 5,000 + ₹ 5,000).

May/June 2005

12. A firm's balance sheet at the end of 3/04/2022 is: Capital ₹1,00,000, P&L account ₹10,000, Cash ₹95,000, and Fixed assets ₹15,000. On 4/04/2022, the proprietor withdraws ₹10,000 of capital. How is this transaction classified?
(A) As an operating activity
(B) As a financing activity
(C) As an investing activity
(D) As a non-cash transaction

Ans :

(B) As a financing activity
The withdrawal of capital by the proprietor is a transaction that affects the size and composition of the entity's contributed equity. Activities that result in changes to the equity and borrowings of the entity are classified as financing activities. This cash outflow of ₹10,000 directly reduces the firm's capital structure and is therefore a financing activity.

Oct/Nov 2011

13. Which of the following best defines 'Operating activities' in the context of a cash flow statement?
(A) Activities exclusively involving the acquisition and subsequent disposal of long-term operational and financial assets.
(B) Activities resulting in changes to the size and composition of an entity's capital structure, including equity and borrowings.
(C) The principal revenue-producing activities and any other activities that are not classified as investing or financing.
(D) Transactions limited to cash and equivalents which are designated as non-operational and have no impact on reported net profit.

Ans :

(C) The principal revenue-producing activities and any other activities that are not classified as investing or financing.
Operating activities are the core business functions that generate revenue for an entity. This category includes all transactions and events that are not defined as investing or financing

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activities. They primarily consist of cash inflows and outflows resulting from transactions that directly affect the firm's net profit or loss, such as sales and purchases of goods.

May/June 2024

14. Identify the activity that falls under the category of 'Investing activities' in a cash flow statement.
(A) Cash received from the sale of goods
(B) Cash paid to employees for salaries
(C) Cash proceeds from issuing new shares
(D) Cash payment for the acquisition of long-term assets

Ans :

(D) Cash payment for the acquisition of long-term assets
Investing activities include the purchase and sale of long-term assets and other investments not classified as cash equivalents. The acquisition of assets like machinery, buildings, or intangible assets represents a cash outflow for resources intended to generate future income. Therefore, cash payment for such acquisitions is a classic example of an investing activity.

Oct/Nov 2016

15. Which of the following is a defining characteristic of 'Financing activities'?
(A) They result in changes in the size and composition of the contributed equity and borrowings.
(B) They consist of the primary revenue-generating operations central to the entity's business model.
(C) They involve the purchase and sale of long-term assets intended to generate future economic benefits.
(D) They are transactions directly used in the calculation of the net profit or loss figure for the period.

Ans :

(A) They result in changes in the size and composition of the contributed equity and borrowings.
Financing activities are transactions with the owners and creditors of the company. These activities involve obtaining resources from and returning resources to them. Examples include issuing or buying back shares, and taking or repaying loans. Consequently, they directly alter the makeup of the entity's equity capital and debt structure.

May/June 2020

16. When calculating cash flow from operating activities, how does an increase in current assets (other than cash) affect the cash position?
(A) It has no impact on the cash position.
(B) It represents a consumption or use of cash.
(C) It represents a generation of cash.
(D) It is treated as a financing activity.

Ans :

(B) It represents a consumption or use of cash.
An increase in current assets other than cash, such as inventory or accounts receivable, signifies that cash has been used or "blocked." For example, buying more inventory consumes cash, and making sales on credit increases receivables instead of cash. Therefore, such an increase reduces the cash available from operating activities and is considered a use of cash.

Oct/Nov 2019

17. How does an increase in current liabilities typically affect the cash flow from operating activities?
(A) It results in a consumption of cash.
(B) It results in a generation of cash.
(C) It is classified as an investing activity.
(D) It has no effect on the cash flow.

Ans :

(B) It results in a generation of cash.
An increase in current liabilities, such as bills payable, indicates that the company has received goods or services without an immediate cash payment, effectively conserving its cash. This delay in payment acts as a source of short-term financing from suppliers, thus representing a generation of cash from an operational perspective and increasing the cash flow from operating activities.

May/June 2013

18. If the value of (current assets other than cash minus current liabilities) shows an increase over a period, what does this imply for cash flow from operating activities?
(A) Cash inflows from operations are reduced as cash is blocked in working capital.
(B) Operating cash inflows are augmented by the exact amount of this working capital change.

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CHAPTER 16

Cash Flow and Funds Flow

Oct/Nov 2018

1. According to the introductory principles of cash flow, what is the primary role of cash in a business enterprise?

(A) To maximize long-term profitability and shareholder returns

(B) To provide the necessary liquidity for smooth daily operations

(C) To serve as the main indicator of an enterprise's market value

(D) To exclusively fund large-scale expansion and capital projects

Ans :

(B) To provide the necessary liquidity for smooth daily operations

Cash is fundamentally important as it enables an enterprise to conduct its daily operations without disruption. It provides the essential liquidity required to meet short-term obligations and maintain business continuity. While profit is the main objective, sufficient cash is necessary to sustain operations, purchase commodities, and manage day-to-day expenses, ensuring the business runs smoothly.

May/June 2021

2. Which of the following statements accurately distinguishes between profit and cash generation in a business?

(A) A firm can report a profit for a period but have less cash at the end than at the beginning.

(B) Profit and cash generation are always identical in any given accounting period under all circumstances.

(C) A firm that generates a positive cash flow for a period is always guaranteed to be profitable in that period.

(D) Profit is calculated on a cash basis, while cash generation is calculated on an accrual basis.

Ans :

(A) A firm can report a profit for a period but have less cash at the end than at the beginning.

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Profit is not the same as cash generation. An enterprise can be profitable on paper, for instance, by selling goods on credit at a high margin. However, if the cash from these sales is not collected, the firm's cash position can worsen despite the recorded profit, highlighting the critical difference between accrual-based profit and actual cash flow.

Oct/Nov 2005

3. What defines 'cash equivalents' as per the principles of cash flow statement preparation?

(A) Long-term investments, such as stocks or bonds, held for capital appreciation over a period exceeding one year.

(B) All assets listed on the balance sheet, including less liquid items like raw material inventory and non-current fixed assets.

(C) Short-term, highly liquid investments readily convertible to a known amount of cash with insignificant risk of value change.

(D) Restricted cash or funds held in special escrow accounts to fulfill specific, long-term contractual or legal obligations.

Ans :

(C) Short-term, highly liquid investments readily convertible to a known amount of cash with insignificant risk of value change.

Cash equivalents are specifically defined as investments that are short-term and highly liquid. The key characteristics are their easy convertibility into a known, predictable amount of cash and their exposure to a negligible risk of fluctuation in value. This distinguishes them from other types of investments that may have higher risk or longer maturity periods.

May/June 2014

4. What is the primary purpose of preparing a cash flow statement for an enterprise?

(A) To calculate a precise market valuation of the company's equity shares for use by potential and current investors.

(B) To serve as a comprehensive replacement

2 is incorrect; income tax payments are usually classified as operating activities unless they can be specifically identified with financing or investing activities, which is an exception, not the rule.

Oct/Nov 2013

23. Why might an enterprise with consistently high positive cash flows from operating activities choose to engage in investing activities?

(A) To deliberately increase the balance of its short-term liabilities, such as accounts payable.
(B) To execute a plan to reduce its total amount of contributed equity capital.
(C) To ensure sufficient funds are available to cover routine daily operational expenses.
(D) To deploy unproductive cash balances into assets that can generate future income.

Ans :

(D) To deploy unproductive cash balances into assets that can generate future income.
While cash provides liquidity, holding excessive cash is unproductive as it earns little to no return. An enterprise with strong operating cash flows will seek to invest this surplus cash in fixed or financial assets. These investments are intended to generate future income and cash flows, thereby making productive use of the available funds.

May/June 2010

24. Which of the following transactions would be classified as a cash outflow from an investing activity for a manufacturing company?

(A) Repayment of a long-term bank loan
(B) Purchase of equity shares of a subsidiary company
(C) Payment of salaries to factory workers
(D) Issuance of company debentures for cash

Ans :

(B) Purchase of equity shares of a subsidiary company
Investing activities include the acquisition of long-term assets and other investments. The purchase of equity instruments of another entity, such as a subsidiary, represents an investment made with the intention of generating future returns. For a non-financial company, this is a clear example of an investing cash outflow, distinct from its core operational or financing functions.

Oct/Nov 2015

25. Which of the following represents a cash inflow from an investing activity?

(A) Cash receipts from the sale of property, plant, and equipment
(B) Cash proceeds from issuing debentures
(C) Cash received from customers for services rendered
(D) Cash received from a short-term bank loan

Ans :

(A) Cash receipts from the sale of property, plant, and equipment
Investing activities involve the disposal of long-term assets. When an entity sells its property, plant, or equipment, the cash received from this sale is classified as a cash inflow from investing activities. This represents a conversion of a long-term asset back into cash, which is different from operational revenue or funds raised through financing.

May/June 2009

26. For a non-financial entity, how is the receipt of repayment for a loan previously made to another party classified?

(A) As a financing cash inflow
(B) As an investing cash inflow
(C) As an operating cash inflow
(D) As a non-cash transaction

Ans :

(B) As an investing cash inflow
When a non-financial entity makes a loan to another party, it is classified as an investing outflow. Consequently, when the principal amount of that loan is repaid to the entity, the cash received is classified as an investing inflow. It represents the return on an investment, not a flow from core operations or a financing activity.

Oct/Nov 2022

27. Under what circumstance are cash payments for futures or forward contracts classified as investing activities?

(A) When the contracts are held for dealing or trading purposes
(B) When the payments are classified as financing activities
(C) When the contracts are not held for dealing, trading, or financing purposes
(D) This transaction is always an operating activity

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Ans :

(C) When the contracts are not held for dealing, trading, or financing purposes
Cash flows from derivative contracts like futures and forwards are classified based on their purpose. If they are held for dealing or trading, they are operating activities. If they are part of a financing arrangement, they are financing activities. Only when they do not fall into these two categories are they classified as investing activities.

May/June 2022

28. If a contract is accounted for as a hedge of an identifiable position, how are its cash flows classified?
(A) In the same manner as the cash flows of the position being hedged
(B) Always as operating activities
(C) Always as investing activities
(D) Always as financing activities

Ans :

(A) In the same manner as the cash flows of the position being hedged
When a derivative contract is used for hedging, its accounting treatment follows the item it hedges. The cash flows of the hedging instrument are classified in the same category as the cash flows of the hedged position. For instance, if it hedges an asset acquisition (investing), its cash flows are also classified as investing.

Oct/Nov 2017

29. Which of the following is an example of a cash flow from a financing activity?
(A) Cash payments to acquire intangible assets
(B) Cash receipts from the sale of goods
(C) Cash proceeds from issuing shares or other equity instruments
(D) Cash advances and loans made to other parties by a manufacturing firm

Ans :

(C) Cash proceeds from issuing shares or other equity instruments
Financing activities involve transactions with the owners and lenders of an entity. Issuing new shares to raise capital is a primary example of a financing activity. The cash received from this issuance directly increases the company's equity base and is therefore classified as a cash inflow from financing activities, reflecting a change in its capital structure.

May/June 2019

30. Cash payments made by a company to redeem its own shares are classified as:
(A) An operating cash outflow
(B) An investing cash outflow
(C) A financing cash outflow
(D) A non-cash transaction

Ans :

(C) A financing cash outflow
The redemption or buy-back of an entity's own shares is a transaction with its owners that reduces the contributed equity. Such activities that alter the size and composition of the entity's equity are classified as financing activities. The cash paid to shareholders to acquire these shares constitutes a financing cash outflow.

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Oct/Nov 2020

31. How would the cash proceeds from issuing long-term bonds be classified in a cash flow statement?
(A) As an operating cash inflow
(B) As an investing cash inflow
(C) As a component of cash equivalents
(D) As a financing cash inflow

Ans :

(D) As a financing cash inflow
Issuing bonds, debentures, notes, or taking out loans are methods of raising funds through borrowing. These transactions increase the entity's liabilities and change its capital structure. Therefore, the cash received from such issuances is classified as a cash inflow from financing activities, as it represents funds provided by creditors rather than owners or operations.

May/June 2012

32. A company makes a cash payment for the reduction of the outstanding liability relating to a finance lease. This payment is categorized as:
(A) An operating cash outflow
(B) A financing cash outflow
(C) An investing cash outflow
(D) A miscellaneous cash outflow

Ans :

(B) A financing cash outflow
A finance lease is a form of borrowing to acquire an asset. The liability associated with it is a form

of debt. Therefore, payments made to reduce the principal amount of this outstanding lease liability are treated as repayments of a borrowing. This is classified as a financing cash outflow, similar to repaying a loan.

Oct/Nov 2008

33. According to Ind AS-7, an entity must report cash flows from operating activities using one of two methods. What are these two methods?
(A) The accrual method and the cash method
(B) The gross method and the net method
(C) The direct method and the indirect method
(D) The working capital method and the net profit method

Ans :

(C) The direct method and the indirect method
Ind AS-7 specifies two alternative methods for presenting cash flows from operating activities. The direct method discloses major classes of gross cash receipts and payments. The indirect method starts with net profit or loss and adjusts it for non-cash items and changes in working capital to arrive at the net cash flow from operations.

May/June 2007

34. What is the primary characteristic of the 'direct method' of preparing a cash flow statement as per Ind AS-7?
(A) It starts with net profit and makes adjustments.
(B) It focuses exclusively on changes in working capital.
(C) It is only applicable to financial institutions.
(D) It discloses major classes of gross cash receipts and gross cash payments.

Ans :

(D) It discloses major classes of gross cash receipts and gross cash payments.
The direct method provides a clear summary of actual cash movements by reporting the major categories of cash inflows and outflows directly. For example, it would show "cash received from customers" and "cash paid to suppliers and employees" as separate line items. This approach presents a more straightforward picture of cash generation and usage in operations.

Oct/Nov 2014

35. The 'indirect method' for reporting cash flow from operating activities begins with what figure?
(A) Profit or loss for the period
(B) Gross cash receipts from customers
(C) Total revenue for the period
(D) The opening cash balance

Ans :

(A) Profit or loss for the period
The indirect method reconciles the accrual-based net profit or loss with the cash-based flow from operations. It starts with the net profit or loss figure from the income statement and adjusts it for the effects of non-cash transactions (like depreciation), deferrals or accruals of past or future operating cash flows, and investing or financing items.

May/June 2016

36. How is the purchase of a cash equivalent, such as a 60-day treasury bill, using funds from an entity's bank account treated in the cash flow statement?
(A) As an operating cash outflow
(B) It is excluded from the cash flow statement.
(C) As an investing cash outflow
(D) As a financing cash outflow

Ans :

(B) It is excluded from the cash flow statement.
The purchase of a highly liquid, short-term investment like a 60-day treasury bill is a movement between two components of 'cash and cash equivalents' (e.g., cash at bank and a treasury bill). Such movements are considered part of an entity's cash management, not its operating, investing, or financing activities, and are therefore excluded from the body of the cash flow statement.

Oct/Nov 2006

37. A single transaction, such as the repayment of a loan, may include cash flows that are classified differently. How is a loan repayment consisting of principal and interest typically split?
(A) Both principal and interest are classified as financing activities.
(B) Both principal and interest are classified as operating activities.
(C) The principal is operating, and the interest is classified as a financing activity.
(D) The principal is financing, and the interest may be classified as an operating activity.

Ans :

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(C) This change has no discernible impact on the net cash flow from operating activities.
(D) It signifies a corresponding increase in the net cash flow from financing activities.

Ans :

(A) Cash inflows from operations are reduced as cash is blocked in working capital.
An increase in the net figure of (current assets other than cash minus current liabilities) signifies an increase in net working capital. This growth in working capital requires funding, meaning that cash generated from operations has been consumed or "blocked" to finance this increase. Consequently, the overall cash inflow from operating activities is reduced by this amount.

Oct/Nov 2010

19. Which of the following is NOT an example of a cash flow from operating activities?
(A) Cash receipts from royalties and fees
(B) Cash payments to suppliers for goods and services
(C) Cash receipts from the sale of a manufacturing plant
(D) Cash payments to and on behalf of employees

Ans :

(C) Cash receipts from the sale of a manufacturing plant
The sale of a manufacturing plant is a disposal of a long-term asset. Cash flows related to the acquisition and disposal of long-term assets are classified as investing activities, not operating activities. While rent received from such an asset would be operational, the proceeds from its sale are considered an investing cash inflow.

May/June 2025

20. For a financial institution, how are cash advances and loans made to customers typically classified in the cash flow statement?
(A) As operating activities
(B) As investing activities
(C) As financing activities
(D) As non-cash transactions

Ans :

(A) As operating activities
For a financial institution like a bank, making loans and providing cash advances are part of its main revenue-producing activities. These transactions are central to its core business operations. Therefore, unlike for a non-financial company, the cash flows arising from making loans and receiving repayments are classified under operating activities for a financial institution.

Oct/Nov 2009

21. **Assertion (A) :** Cash payments or refunds of income taxes are generally classified as operating activities.
Reason (R) : Income taxes arise from profits, which are a result of the entity's operating, investing, and financing activities.
(A) Both A and R are true and R is the correct explanation of A.
(B) Both A and R are true but R is not the correct explanation of A.
(C) A is true but R is false.
(D) A is false but R is true.

Ans :

(A) Both A and R are true and R is the correct explanation of A.
Income tax is a direct consequence of an entity's profitability. Since profit is generated through a combination of operating, investing, and financing activities, the resulting tax is fundamentally linked to operations. Unless a tax payment can be specifically tied to a financing or investing transaction, it is classified by default under operating activities.

May/June 2006

22. Consider the following statements regarding cash flows from operating activities:
1. Cash receipts from the sale of goods are an operating cash inflow.
2. Cash payments for income taxes are always classified as investing activities.
3. For a bank, cash advances made to customers are an operating activity.

Which of the statements is/are correct?
(A) 1 only
(B) 1 and 3 only
(C) 2 and 3 only
(D) 1, 2, and 3

Ans :

(B) 1 and 3 only
Statement 1 is correct as sales are a principal revenue-producing activity. Statement 3 is correct because for a financial institution, making loans is a core operational function. Statement

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the fiscal year.

(D) By applying the exchange rate between the functional and foreign currency at the date of the cash flow.

Ans :

(D) By applying the exchange rate between the functional and foreign currency at the date of the cash flow.

According to Ind AS-7, for accuracy, foreign currency cash flows must be translated into the entity's functional currency using the spot exchange rate on the date the cash flow occurs. This ensures that the transaction is recorded at its actual value at that specific point in time, providing a true representation of the cash movement.

May/June 2015

42. According to Ind AS-7, how should cash flows from interest and dividends received and paid be treated?

(A) They are required to be classified exclusively as operating activities in all circumstances.

(B) They should be disclosed separately and classified consistently as operating, investing, or financing.

(C) They are required to be netted against each other and presented as one single line item.

(D) They are omitted from the cash flow statement itself but must be detailed in the notes.

Ans :

(B) They should be disclosed separately and classified consistently as operating, investing, or financing.

Ind AS-7 requires separate disclosure for interest and dividends (both paid and received) to provide clarity. Furthermore, an entity must choose a classification policy (operating, investing, or financing) for these items and apply it consistently from one period to the next to ensure comparability of the financial statements over time.

Oct/Nov 2018

43. An entity capitalises borrowing costs in accordance with Ind AS 23. How is the total interest paid during a period disclosed in the statement of cash flows?

(A) Only the portion recognised as an expense is disclosed.

(B) It is not disclosed in the cash flow statement at all.

(C) The total amount of interest paid is disclosed, regardless of whether it was expensed or capitalised.

(D) Only the capitalised portion is disclosed as an investing activity.

Ans :

(C) The total amount of interest paid is disclosed, regardless of whether it was expensed or capitalised.

Ind AS-7 mandates the disclosure of the total cash outflow for interest paid during the period. This requirement holds true whether the interest has been recognized as an expense in the profit or loss account or has been capitalized as part of the cost of an asset. This provides a complete picture of cash spent on interest.

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May/June 2021

44. Identify the correct statement regarding the classification of cash flows from taxes on income.

(A) They must always be classified as financing activities.

(B) They are netted against tax refunds and not disclosed separately.

(C) They are always classified as investing activities.

(D) They are separately disclosed and generally classified as operating activities.

Ans :

(D) They are separately disclosed and generally classified as operating activities.

Cash flows related to income taxes are required to be disclosed as a separate line item. The standard classification for these flows is under operating activities. An exception exists only if the tax can be specifically and practically identified with a particular financing or investing transaction, in which case it would be classified accordingly.

Oct/Nov 2005

45. How are the aggregate cash flows arising from obtaining or losing control of subsidiaries classified?

(A) As investing activities

(B) As operating activities

(C) As financing activities

(D) As extraordinary items

Ans :

(D) Decrease in equity

Ans :

(C) Increase in long-term borrowings
Long-term sources are funds that are expected to be available to the business for more than one year. An increase in long-term borrowings, such as taking a new term loan, represents a significant injection of funds with a long repayment horizon. This is a classic example of a long-term source, alongside an increase in equity or reserves.

May/June 2012

74. An increase in non-current assets would be classified as what in a funds flow statement?
(A) A long-term source of funds
(B) A short-term source of funds
(C) A short-term use of funds
(D) A long-term use of funds

Ans :

(D) A long-term use of funds
Non-current assets are long-term assets like property, plant, and equipment. An increase in these assets means the company has spent or applied funds to acquire them. Since these assets have a long-term nature, the expenditure is classified as a long-term use of funds, reflecting an investment in the company's long-term operational capacity.

Oct/Nov 2008

75. A decrease in current assets is classified as which of the following in a funds flow statement?
(A) A short-term source of funds
(B) A short-term use of funds
(C) A long-term source of funds
(D) A long-term use of funds

Ans :

(A) A short-term source of funds
Current assets, such as inventory or receivables, are short-term in nature. A decrease in these assets, for instance, by selling inventory for cash or collecting from debtors, releases funds that were tied up in working capital. This release of funds is therefore considered a short-term source of funds for the enterprise.

May/June 2007

76. Identify the transaction that represents a 'Short Term Use' of funds.
(A) Increase in equity
(B) Increase in current assets
(C) Decrease in non-current assets
(D) Increase in long-term borrowings

Ans :

(B) Increase in current assets
An increase in current assets, such as building up inventory or an increase in receivables from credit sales, means that funds have been applied or tied up in short-term operational assets. This application of funds to finance the day-to-day business cycle is classified as a short-term use of funds.

Oct/Nov 2014

77. While preparing a funds flow statement, if a company's fixed asset value remains the same in two successive balance sheets, but depreciation of ₹60,000 was charged, what must be inferred?
(A) There was no transaction related to fixed assets during the year.
(B) Fixed assets of ₹60,000 were sold during the year.
(C) The depreciation charge was incorrect.
(D) Additional fixed assets of ₹60,000 were purchased during the year.

Ans :

(D) Additional fixed assets of ₹60,000 were purchased during the year.
If the closing book value of fixed assets is the same as the opening value after accounting for a depreciation charge of ₹60,000, it implies that new assets must have been purchased. The purchase would have been for an amount equal to the depreciation to offset the reduction, thus indicating a use of funds of ₹60,000.

May/June 2016

78. In the scenario from the previous question (fixed assets unchanged, depreciation of ₹60,000), how should this be reflected in the funds flow statement?
(A) Both as a source (depreciation/funds from operations) and a use (purchase of assets) of ₹60,000.
(B) As a source of funds of ₹60,000 only.
(C) As a use of funds of ₹60,000 only.
(D) It should be ignored as there is no net change.

Ans :

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May/June 2017

50. In the operating activities section of a cash flow statement (indirect method), what adjustment is made for a decrease in accounts receivable?
(A) The decrease is added to operating income.
(B) The decrease is subtracted from operating income.
(C) The decrease is classified as a financing inflow.
(D) No adjustment is made for changes in accounts receivable.

Ans :

(A) The decrease is added to operating income.
A decrease in accounts receivable means that the company collected more cash from customers than the revenue it recorded on a credit basis during the period. This represents an additional cash inflow compared to the accrual-based profit figure. Therefore, the amount of the decrease is added back to operating income to reflect this positive cash impact.

Oct/Nov 2021

51. How is a decrease in accounts payable adjusted in the operating activities section when using the indirect method?
(A) It is added to operating income.
(B) It is shown as a financing outflow.
(C) It is shown as an investing outflow.
(D) It is subtracted from operating income.

Ans :

(D) It is subtracted from operating income.
A decrease in accounts payable signifies that the company paid off its suppliers at a faster rate than it incurred new credit purchases. This results in a cash outflow that is greater than the expenses recorded on an accrual basis. To reflect this use of cash, the amount of the decrease is subtracted from the operating income.

May/June 2011

52. Match List-I with List-II regarding adjustments for operating activities under the indirect method.
List-I (Change in Item)
P. Increase in Accounts Receivable
Q. Decrease in Other Current Assets
R. Increase in Accounts Payable
S. Decrease in Other Current Liabilities
List-II (Adjustment to Operating Income)
1. Add
2. Subtract
3. Subtract
4. Add
(A) P-2, Q-4, R-4, S-3
(B) P-3, Q-1, R-1, S-2
(C) P-2, Q-1, R-4, S-3
(D) P-3, Q-4, R-1, S-2

Ans :

(A) P-2, Q-4, R-4, S-3
P-Increase in receivables is a use of cash (Subtract). Q-Decrease in other current assets releases cash (Add). R-Increase in payables is a source of cash (Add). S-Decrease in other current liabilities is a use of cash (Subtract). The standard adjustments reflect whether a change in working capital items consumed or generated cash during the period.

Oct/Nov 2007

53. Which of the following transactions would appear in the 'Cash flows from Investing Activities' section of a cash flow statement?
(A) Payment of dividend
(B) Decrease in borrowings
(C) Purchase of long-term assets
(D) Increase in equity

Ans :

(C) Purchase of long-term assets
The investing activities section reports cash flows related to the acquisition and disposal of long-term assets and other investments. The purchase of long-term assets, such as machinery or buildings, is a primary example of a cash outflow from investing activities. The other options relate to financing activities (dividend, equity, borrowings).

May/June 2005

54. In the indicative format of a cash flow statement, 'Payment of dividend' is classified under which category?
(A) Operating Activities
(B) Investing Activities
(C) Non-cash Activities
(D) Financing Activities

Ans :

(D) Financing Activities
Payment of dividends is a return of capital to the shareholders (owners) of the entity. Transactions with owners that affect the entity's capital structure are classified as financing activities.

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Ans :

(C) A financing cash outflow
The withdrawal of capital by the proprietor is a transaction with an owner that reduces the entity's equity. Activities that change the size and composition of contributed equity are classified as financing activities. Therefore, this ₹10,000 payment to the owner is a financing cash outflow, representing a return of capital to the provider.

May/June 2015

84. What is the total net cash flow for a firm on 4/04/2022, considering a net operating inflow of ₹5,000 and a capital withdrawal of ₹10,000?
(A) A net cash inflow of ₹5,000
(B) A net cash outflow of ₹15,000
(C) A net cash outflow of ₹10,000
(D) A net cash outflow of ₹5,000

Ans :

(D) A net cash outflow of ₹5,000
On 4/04/2022, there was a net cash inflow from operating activities of ₹5,000. There was also a cash outflow from financing activities of ₹10,000 due to the capital withdrawal. The total net cash flow for the day is the sum of these flows (+₹ 5,000 - ₹ 10,000), which results in a net outflow of ₹5,000.

Oct/Nov 2018

85. If a firm's P&L account was ₹10,000 at the start of 4/04/2022 and its only profit-related transaction was earning a ₹5,000 profit from trading, what is the change in the P&L account balance?
(A) An increase of ₹5,000
(B) An increase of ₹10,000
(C) A decrease of ₹5,000
(D) No change

Ans :

(A) An increase of ₹5,000
The only transaction affecting profit on 4/04/2022 was the trading of wheat. The firm bought wheat for ₹75,000 and sold it for ₹80,000, generating a profit of ₹5,000. This profit is added to the P&L account, increasing its balance from ₹10,000 at the start of the day to ₹15,000 by the end.

May/June 2021

86. Given a cash balance of ₹95,000 at the start of 4/04/2022 and a net cash outflow of ₹5,000 for the day, what is the calculated closing cash balance, and does it match a balance sheet figure of ₹90,000?
(A) ₹1,00,000; it does not match.
(B) ₹90,000; it matches the balance sheet figure.
(C) ₹85,000; it does not match.
(D) ₹95,000; it matches the balance sheet figure.

Ans :

(B) ₹90,000; it matches the balance sheet figure.
The opening cash was ₹95,000. The day's net cash flow was an outflow of ₹5,000 (+₹ 5,000 from operations, -₹ 10,000 from financing). The calculated closing cash is ₹ 95,000 - ₹ 5,000 = ₹ 90,000. This amount correctly matches the cash balance of ₹90,000 shown in the balance sheet as at the end of 4/04/2022.

Oct/Nov 2005

87. **Assertion (A) :** A continuously loss-making enterprise will not be able to sustain its operation for very long.
Reason (R) : Profit is the same as cash generation, and losses directly deplete cash reserves.
(A) Both A and R are true and R is the correct explanation of A.
(B) Both A and R are true but R is not the correct explanation of A.
(C) A is true but R is false.
(D) A is false but R is true.

Ans :

(C) A is true but R is false.
Assertion (A) is true because sustained losses erode an enterprise's capital base, making it unviable. However, Reason (R) is false. Profit is not the same as cash generation. A firm can be profitable yet face a cash crunch, or vice versa. The reason for unsustainability is the erosion of net worth, not a direct equivalence between loss and cash.

May/June 2014

88. Which of the following statements about the three categories of cash flow activities is correct?
(A) Operating activities are those that are not investing or financing activities.
(B) Operating activities relate to changes in long-term assets.
(C) Investing activities relate to changes in equity and borrowings.
(D) Financing activities are the principal revenue-producing activities.

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(C) To assess the liquidity position and ability to pay its debts

For a supplier, the primary concern is whether their customer can pay for goods and services provided. The cash flow statement provides crucial insights into the customer's liquidity and its ability to generate sufficient cash to meet its short-term obligations. This helps the supplier evaluate credit risk and make informed decisions about credit terms.

May/June 2013

60. How do bankers and other creditors typically use cash flow information?

(A) To determine repayment schedules for loans and stipulate covenants on expenses and investments

(B) To formulate and decide upon the optimal marketing strategy for the company's main products.

(C) To perform an assessment of the company's adherence to relevant environmental laws and regulations.

(D) To manage the human resources process of recruiting and hiring new employees for the company.

Ans :

(A) To determine repayment schedules for loans and stipulate covenants on expenses and investments

Bankers and creditors analyze cash flow information to gauge a borrower's ability to service debt. This analysis helps in structuring loan repayment schedules that align with the company's cash generation cycle. They may also impose covenants, which are restrictions on certain expenses or investments, to protect their interests and ensure loan repayment capacity is maintained.

Oct/Nov 2010

61. What is the fundamental difference between a cash flow statement prepared for statutory reporting and a cash budget prepared for assessing working capital needs from a bank?

(A) The statutory statement must use the direct method, whereas the bank budget must use the indirect method.

(B) The statutory statement reports on historical periods, while the bank budget exclusively projects future periods.

(C) The statutory statement's main focus is working capital, while the bank budget's primary focus is net profit.

(D) The bank budget takes all cash flows excluding bank finance to find the deficit, which forms the basis for the loan.

Ans :

(D) The bank budget takes all cash flows excluding bank finance to find the deficit, which forms the basis for the loan.

A cash budget prepared for a bank loan projects all expected cash inflows and outflows for a future period. Crucially, it excludes potential bank finance from the inflows. The resulting projected deficit or shortfall represents the company's need for working capital funds, which then becomes the basis for the bank to assess and grant a loan.

May/June 2025

62. In the context of a funds flow statement, how are items on the liabilities side of a balance sheet generally interpreted?

(A) As a use of funds

(B) As a source of funds

(C) As non-fund items

(D) As unutilized funds

Ans :

(B) As a source of funds

The liabilities and equity side of a balance sheet represents the claims of outsiders and owners on the firm's assets. These items, such as capital, reserves, and loans, signify the funds that have been provided to the enterprise to acquire its assets. Therefore, they are fundamentally considered sources of funds for the business.

Oct/Nov 2009

63. When comparing two balance sheets to prepare a funds flow statement, what does an increase in an item on the liabilities side signify?

(A) An additional use of funds

(B) A decrease in working capital

(C) An additional source of funds

(D) No change in the fund position

Ans :

(C) An additional source of funds

An increase in a liability or equity item between two balance sheet dates, such as an increase in long-term borrowings or share capital, means that more funds have been made available to

NODIA

Therefore, the cash outflow for dividend payments is reported in the financing activities section of the cash flow statement, as a use of funds.

Oct/Nov 2011

55. An increase in equity capital from the issuance of new shares would be shown as:
(A) A positive item under Financing Activities
(B) A negative item under Financing Activities
(C) A positive item under Investing Activities
(D) An adjustment in Operating Activities

Ans :

(A) A positive item under Financing Activities
An increase in equity results from issuing new shares, which brings cash into the company from its owners. This transaction directly impacts the entity's capital structure and is a source of funds. Therefore, it is recorded as a positive cash flow (inflow) under the financing activities section of the cash flow statement.

May/June 2024

56. How is a decrease in borrowings (e.g., repayment of a loan) reflected in the financing activities section?
(A) As a positive item (+)
(B) As a negative item (-)
(C) It is not shown in the financing section.
(D) It is added to operating income.

Ans :

(B) As a negative item (-)
A decrease in borrowings signifies the repayment of debt to lenders. This is a cash outflow from the company to its creditors, reducing its financial liabilities. Consequently, this transaction is shown as a negative item, or a use of cash, within the financing activities section of the cash flow statement, reflecting a reduction in debt.

Oct/Nov 2016

57. After calculating the net cash flows from operating, investing, and financing activities, what is typically deducted to arrive at the net cash flow of the entity?
(A) Depreciation and amortization
(B) Proceeds from sale of assets
(C) Payment of interest and taxes
(D) Increase in equity

Ans :

(C) Payment of interest and taxes
In the indicative format, the net cash flows from the three main activities are summed up. From this sub-total, cash payments for interest and taxes are deducted to determine the final net cash flow for the entity during the period. This presentation provides a clear picture of cash generated before and after these significant obligations.

May/June 2020

58. Which of the following is a key benefit of cash flow information when used with other financial statements?
(A) It allows users to evaluate changes in net assets, financial structure, and the ability to adapt to changing circumstances.
(B) It provides a definitive guarantee of the enterprise's future profitability and success.
(C) It offers a precise and conclusive valuation of the company's intangible assets like brand and goodwill.
(D) It serves as a substitute for and eliminates the requirement of an independent audit of financial statements.

Ans :

(A) It allows users to evaluate changes in net assets, financial structure, and the ability to adapt to changing circumstances.
A cash flow statement, in conjunction with the balance sheet and income statement, provides a holistic view of an entity's performance. It helps users assess its financial structure, including liquidity and solvency, and its capacity to manage cash flows to respond to opportunities and challenges, thereby offering a dynamic perspective on financial health.

Oct/Nov 2019

59. How can suppliers use an enterprise's cash flow information?
(A) To determine the dividend policy of the enterprise
(B) To calculate the P/E ratio of the enterprise's stock
(C) To assess the liquidity position and ability to pay its debts
(D) To set the salaries for the enterprise's top management

Ans :

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Ans :

(A) A Cash Flow Statement determines changes in working capital over a period.
A Cash Flow Statement determines the net change in cash and cash equivalents, leading to the cash position at the end of the period. It is the Funds Flow Statement that is primarily concerned with analyzing the changes in working capital over a specified period, not the Cash Flow Statement, which has a narrower focus on cash.

Oct/Nov 2022

69. A Cash Flow Statement helps in understanding the business's _____, while a Funds Flow Statement helps in assessing its _____.
(A) long-term strategy, liquidity position
(B) accrual accounting, cash accounting
(C) liquidity position, long-term financial strategy
(D) market share, production efficiency

Ans :

(C) liquidity position, long-term financial strategy
The Cash Flow Statement provides a detailed view of the cash inflows and outflows, which is crucial for evaluating the short-term liquidity and solvency of a business. In contrast, the Funds Flow Statement offers a broader perspective on how funds are sourced and utilized, which is more useful for assessing the long-term financial strategy and structural changes.

May/June 2022

70. Which accounting system is associated with the Funds Flow Statement?
(A) Accrual system of accounting
(B) Cash system of accounting
(C) Hybrid system of accounting
(D) It does not use any formal accounting system.

Ans :

(A) Accrual system of accounting
The Funds Flow Statement is based on the concept of working capital, which includes non-cash items like receivables, payables, and inventory. Its preparation involves analyzing changes in balance sheet items that are recorded using the accrual system of accounting. The Cash Flow Statement, by contrast, is more aligned with the cash basis of accounting.

NODIA

Oct/Nov 2017

71. For the purpose of preparing a funds flow statement, information is organized into which two principal groups?
(A) Inflows and Outflows
(B) Long-term and Short-term
(C) Operating and Non-operating
(D) Sources of funds and applications of funds

Ans :

(D) Sources of funds and applications of funds
The fundamental structure of a funds flow statement involves categorizing all changes in the financial position between two dates into two main groups. These are the 'sources of funds,' which details where financial resources came from, and the 'applications (or uses) of funds,' which shows how those resources were employed by the enterprise.

May/June 2019

72. In a banker's format for a funds flow statement, why are sources and uses often further classified into 'Long term' and 'Short term'?
(A) To ensure full compliance with all relevant international accounting and reporting standards.
(B) To enable them to know if long-term funds have been diverted for short-term uses.
(C) To accurately calculate the final net profit figure for the reporting period.
(D) To compute the precise cash and cash equivalents balance at the end of the period.

Ans :

(B) To enable them to know if long-term funds have been diverted for short-term uses.
Bankers use this specific format to assess the financial discipline of a borrower. A key concern is the mismatch of funds. By segregating sources and uses into long-term and short-term, a banker can quickly identify if funds raised for long-term purposes (like a term loan for machinery) have been improperly used to fund short-term needs (like daily operations).

Oct/Nov 2020

73. Which of the following would be considered a 'Long Term Source' of funds in a typical funds flow statement?
(A) Decrease in current assets
(B) Increase in short-term borrowings
(C) Increase in long-term borrowings

(A) As investing activities
The acquisition or disposal of subsidiaries or other business units is considered a major strategic investment or divestment decision. Therefore, the associated aggregate cash flows are presented separately within the cash flow statement and are classified as investing activities, reflecting the long-term resource allocation choices made by the management of the entity.

May/June 2014

46. What is the treatment for investing and financing transactions that do not require the use of cash or cash equivalents?
(A) They must be included in the cash flow statement within their appropriate activity categories.
(B) They are excluded from the cash flow statement but disclosed elsewhere in the financial statements.
(C) They are to be ignored entirely and excluded from all forms of financial reporting.
(D) They must be reported as a specific reconciliation item at the end of the cash flow statement.

Ans :

(B) They are excluded from the cash flow statement but disclosed elsewhere in the financial statements.
The cash flow statement is designed to report only transactions involving cash and cash equivalents. Non-cash transactions, such as acquiring an asset by issuing shares, are excluded from the body of the statement. However, because they are significant investing and financing activities, they must be disclosed in the notes to the financial statements.

Oct/Nov 2023

47. What reconciliation must an entity present in relation to its cash flow statement?
(A) A reconciliation of operating profit with net profit
(B) A reconciliation of total assets with total liabilities
(C) A reconciliation of direct method cash flows with indirect method cash flows
(D) A reconciliation of the amounts in its statement of cash flows with the equivalent items in the balance sheet

Ans :

(D) A reconciliation of the amounts in its statement of cash flows with the equivalent items in the balance sheet
To ensure integrity and linkage between financial statements, Ind AS-7 requires an entity to provide a reconciliation. This reconciliation connects the components of 'cash and cash equivalents' as reported at the beginning and end of the cash flow statement with the corresponding line items reported in the balance sheet, ensuring consistency across reports.

May/June 2008

48. In the indicative format for preparing a cash flow statement (indirect method), how is depreciation treated under operating activities?
(A) It is added back to operating income (EBIT).
(B) It is subtracted from operating income.
(C) It is ignored as it is a non-cash item.
(D) It is shown under investing activities.

Ans :

(A) It is added back to operating income (EBIT).
The indirect method starts with profit (like EBIT), which has been reduced by non-cash expenses such as depreciation. To find the actual cash flow, the effect of this non-cash charge must be reversed. Therefore, depreciation is added back to the operating income to nullify its impact and move closer to the cash-based operational result.

Oct/Nov 2012

49. When using the indirect method, how is a loss on the sale of a long-term asset treated to calculate cash flow from operating activities?
(A) It is subtracted from operating income.
(B) It is shown as a financing cash outflow.
(C) It is added back to operating income.
(D) It is ignored in the operating activities section.

Ans :

(C) It is added back to operating income.
A loss on the sale of an asset reduces the reported net income but does not involve an operating cash outflow. The actual cash effect of the sale is fully captured as an investing inflow. To prevent double-counting and to reverse the non-operating impact on profit, this loss is added back in the operating activities section.

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(A) Both as a source (depreciation/funds from operations) and a use (purchase of assets) of ₹60,000.

The depreciation of ₹60,000 is a non-fund expense and is added back to profit to calculate funds from operations, making it a source. The inferred purchase of new fixed assets for ₹60,000 to maintain the book value is an application or use of funds. Both sides of the transaction must be shown for a complete analysis.

Oct/Nov 2006

79. In a funds flow statement, how is the amount received from the sale of fixed assets treated?

(A) As a use of funds
(B) It is deducted from the funds from operations.
(C) As a source of funds
(D) It is ignored if the asset was fully depreciated.

Ans :

(C) As a source of funds

The sale of a fixed asset, regardless of whether it results in a profit or loss, generates an inflow of funds (usually cash) for the enterprise. This inflow makes resources available for other purposes. Therefore, the proceeds received from the disposal of a fixed asset are always treated as a source of funds.

May/June 2023

80. When analyzing the change in Net Worth for a funds flow statement, how should a dividend payment be treated?

(A) It should be shown as a use of funds.
(B) It should be shown as a source of funds.
(C) It should be ignored as it relates to prior year profits.
(D) It should be added back to the opening reserves.

Ans :

(A) It should be shown as a use of funds.

A dividend payment is a distribution of profits to shareholders. This represents an outflow of the company's financial resources. In a funds flow statement, the entire net profit for the year is considered a source of funds, and the portion of that profit distributed as dividends is separately shown as an application or use of funds.

Oct/Nov 2024

81. If a company reduces its equity capital through a share buy-back, how is this reflected in a funds flow analysis?

(A) The net profit figure must be reduced by the buy-back cost before it can be shown as a source.
(B) The total amount spent on the share buy-back is to be presented as a source of funds.
(C) The transaction should be completely ignored in the statement as it is an internal equity adjustment.
(D) The entire net profit is shown as a source, and the buy-back is shown as a use.

Ans :

(D) The entire net profit is shown as a source, and the buy-back is shown as a use.

For a clear analysis, the gross figures are preferred. The total net profit generated during the year is a primary source of funds for the business. The decision to use a portion of these or other funds to buy back shares is a separate application of funds (a use). This method correctly separates fund generation from fund application.

May/June 2018

82. On 4/04/2022, a firm buys wheat for ₹75,000 and sells it for ₹80,000 cash. Based on these transactions, what is the net cash flow from operating activities on that day?

(A) A cash outflow of ₹5,000
(B) A cash inflow of ₹5,000
(C) A cash inflow of ₹80,000
(D) A cash outflow of ₹10,000

Ans :

(B) A cash inflow of ₹5,000

The operating activities on this day are the purchase of wheat for ₹75,000 (outflow) and the sale of wheat for ₹80,000 (inflow). The net cash flow from these principal revenue-producing activities is an inflow of ₹5,000 (₹ 80,000 - ₹ 75,000). This represents the cash generated from the core business trading on that day.

Oct/Nov 2025

83. A proprietor's withdrawal of ₹10,000 capital on 4/04/2022 results in what type of cash flow?

(A) An operating cash outflow
(B) An investing cash outflow
(C) A financing cash outflow
(D) An operating cash inflow

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the enterprise during that period. This inflow of resources is therefore treated as an additional source of funds in the funds flow statement.

May/June 2006

64. In the preparation of a funds flow statement, what does a decrease in an item on the assets side represent?
(A) An additional use of funds
(B) A non-fund transaction
(C) A decrease in long-term liabilities
(D) An additional source of funds

Ans :

(D) An additional source of funds
A decrease in an asset, for example, through the sale of machinery or a reduction in inventory, releases cash or funds that were previously tied up in that asset. This release of funds makes them available for other purposes within the business. Consequently, a decrease in an asset is considered a source of funds.

Oct/Nov 2013

65. What does an increase in an item on the assets side signify in a funds flow analysis?
(A) An additional use of funds
(B) An additional source of funds
(C) A decrease in liabilities
(D) An increase in shareholder's equity

Ans :

(A) An additional use of funds
An increase in an asset, such as the purchase of new equipment or an increase in accounts receivable, means that the enterprise has applied or used its funds to acquire that asset or extend more credit. This application of resources to expand the asset base is categorized as an additional use of funds during the period.

May/June 2010

66. A statement that details the additional sources and uses of funds between two balance sheet dates is known as a:
(A) Cash Budget
(B) Funds Flow Statement
(C) Statement of Retained Earnings
(D) Trial Balance

Ans :

(B) Funds Flow Statement
A funds flow statement is specifically designed to analyze the changes in a company's financial position between two balance sheet dates. It systematically lists all the sources from which funds were generated (e.g., profits, new loans) and all the applications or uses to which those funds were put (e.g., asset purchases, dividend payments).

Oct/Nov 2015

67. Which of the following is a key difference between a Cash Flow Statement and a Funds Flow Statement?
(A) A Cash Flow Statement is an optional report, whereas a Funds Flow Statement is a mandatory filing.
(B) A Cash Flow Statement is based on the accrual system, while a Funds Flow Statement is based on the cash system.
(C) A Cash Flow Statement finds working capital changes, while a Funds Flow Statement finds the final cash position.
(D) A Cash Flow Statement segregates flows into operating, investing, and financing activities, while a Funds Flow Statement does not.

Ans :

(D) A Cash Flow Statement segregates flows into operating, investing, and financing activities, while a Funds Flow Statement does not.
A defining feature of the Cash Flow Statement, as mandated by accounting standards, is its structured presentation of cash flows into three distinct categories: operating, investing, and financing. The Funds Flow Statement, on the other hand, typically classifies fund movements into sources and uses, without this specific three-way segregation of activities.

May/June 2009

68. Identify the incorrect statement from the following comparisons between Cash Flow and Funds Flow statements.
(A) A Cash Flow Statement determines changes in working capital over a period.
(B) A Cash Flow Statement is an integral and mandatory part of financial statements.
(C) A Funds Flow Statement helps in assessing the long-term financial strategy of a business.
(D) A Funds Flow Statement is not a mandatory requirement and not part of the primary financial statements.

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Ans :

(A) Operating activities are those that are not investing or financing activities.
The definitions of the three categories are mutually exclusive. Operating activities are defined as the principal revenue-producing activities of the entity and, by exclusion, any other activities that do not meet the definition of investing (acquisition/disposal of long-term assets) or financing (changes in equity and borrowings) activities, providing a catch-all for core business operations.

Oct/Nov 2023

89. Consider the following cash flow items:
1. Cash paid to suppliers
2. Cash received from sale of equipment
3. Cash proceeds from a bank loan
4. Cash paid for employee salaries

Which of these are classified as cash flows from operating activities?
(A) 1 and 2 only
(B) 3 and 4 only
(C) 1 and 4 only
(D) 2 and 3 only

Ans :

(C) 1 and 4 only
Cash paid to suppliers (1) and cash paid for employee salaries (4) are directly related to the principal revenue-producing activities and are therefore operating cash flows. The sale of equipment (2) is an investing activity, and the proceeds from a bank loan (3) is a financing activity, as it relates to borrowing.

May/June 2008

90. A decrease in working capital (where working capital is defined as current assets other than cash minus current liabilities) over a period implies that:
(A) Cash has been released from working capital, increasing operating cash inflows.
(B) Cash inflows from operating activities are reduced.
(C) The company has made significant long-term investments.
(D) The company has issued a large amount of new equity.

Ans :

(A) Cash has been released from working capital, increasing operating cash inflows.
A decrease in net working capital means that the company has either reduced its current assets (like inventory) or increased its current liabilities (like payables). Both scenarios result in a release of cash that was previously tied up. This release of cash increases the net cash flow generated from the company's operating activities during the period.

Oct/Nov 2012

91. Which of these transactions would be classified as an investing activity for a retail company?
(A) Receiving rent from a sub-let property owned by the company.
(B) Selling shares held for trading purposes.
(C) Paying income tax.
(D) Purchasing a new delivery van.

Ans :

(D) Purchasing a new delivery van.
The purchase of a delivery van represents the acquisition of a long-term asset (property, plant, and equipment) intended to be used in the business. This is a classic investing activity. Rent received and selling trading securities are operating activities, and paying income tax is also generally classified as an operating activity.

May/June 2017

92. Identify the item that is NOT a cash flow from a financing activity.
(A) Cash repayments of amounts borrowed
(B) Cash payments to acquire the entity's own shares
(C) Cash payments to acquire debentures of another entity
(D) Cash proceeds from issuing debentures

Ans :

(C) Cash payments to acquire debentures of another entity
Acquiring the debentures (debt instruments) of another entity is an investment. It is a use of cash to purchase a financial asset with the expectation of future returns (interest and principal). Therefore, this is classified as an investing activity, not a financing activity. The other options all relate to changes in the entity's own capital structure.

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(B) Statement II is correct, but Statement I is incorrect.
(C) Both statements are correct.
(D) Both statements are incorrect.

Ans :

(A) Statement I is correct, but Statement II is incorrect.
Statement I is correct; accounting standards mandate the preparation of a cash flow statement. Statement II is incorrect; a funds flow statement is used to assess long-term financial strategy and changes in working capital, whereas the cash flow statement is the tool primarily used for understanding the short-term liquidity position of a business.

May/June 2022

112. **Assertion (A) :** The cash flow statement is considered more useful for short-term liquidity analysis than the funds flow statement.
Reason (R) : The cash flow statement focuses narrowly on inflows and outflows of cash and cash equivalents, which are the most liquid assets.
(A) Both A and R are true and R is the correct explanation of A.
(B) Both A and R are true but R is not the correct explanation of A.
(C) A is true but R is false.
(D) A is false but R is true.

Ans :

(A) Both A and R are true and R is the correct explanation of A.
Assertion A is correct because liquidity is about meeting immediate obligations with cash. Reason R correctly explains this by stating that the cash flow statement's specific focus on actual cash movements provides the most direct measure of a firm's ability to generate cash. The funds flow statement's broader 'working capital' concept is less precise for immediate liquidity assessment.

Oct/Nov 2017

113. An increase in Reserves in a funds flow statement is classified as a:
(A) Long-term use
(B) Short-term use
(C) Long-term source
(D) Short-term source

Ans :

(C) Long-term source
An increase in reserves typically arises from retaining profits within the business instead of distributing them. These retained earnings are a form of internal financing, providing funds for long-term growth and stability. Therefore, an increase in reserves is classified as a long-term source of funds for the enterprise.

May/June 2019

114. Which of the following is NOT a source of funds in a funds flow statement?
(A) Increase in short term borrowings
(B) Decrease in current assets
(C) Increase in equity
(D) Increase in non-current assets

Ans :

(D) Increase in non-current assets
An increase in non-current assets, such as the purchase of new plant and machinery, requires an expenditure or application of the company's funds. Therefore, it is classified as a use of funds, specifically a long-term use. All the other options represent ways in which funds are made available to the enterprise, making them sources.

Oct/Nov 2020

115. When preparing cash and funds flow statements, why is special care needed for an item like depreciation?
(A) Because it is a non-fund/non-cash item that affects reported profit but not the fund/cash position directly.
(B) Because it is an expense that represents a direct and immediate outflow of cash.
(C) Because it is required to be classified as a cash flow from a financing activity.
(D) Because it must always be classified as a cash flow from an investing activity.

Ans :

(A) Because it is a non-fund/non-cash item that affects reported profit but not the fund/cash position directly.
Depreciation is an accounting entry that reduces profit but does not involve an actual outflow of cash or funds. When preparing cash or funds flow statements that start from profit, depreciation must be added back to reverse its non-cash impact and arrive at the true flow of funds or cash from operations.

NODIA

Oct/Nov 2011

97. Which of the following is considered a 'Long Term Use' of funds in a funds flow statement prepared for a banker?
(A) Increase in Reserves
(B) Decrease in Non-current assets
(C) Increase in Short-term borrowings
(D) Decrease in long-term borrowings

Ans :

(D) Decrease in long-term borrowings
A decrease in long-term borrowings means the company has used its funds to repay a portion of its long-term debt. This application of funds to reduce a long-term liability is classified as a long-term use of funds. An increase in reserves or decrease in non-current assets are sources, and an increase in short-term borrowings is a short-term source.

May/June 2024

98. From the perspective of a funds flow statement, identify the correct pair.
(A) Increase in non-current assets : Use of funds
(B) Increase in equity : Use of funds
(C) Decrease in current assets : Use of funds
(D) Decrease in reserves : Source of funds

Ans :

(A) Increase in non-current assets : Use of funds
An increase in non-current assets, such as purchasing new machinery, requires the application or use of funds. An increase in equity is a source. A decrease in current assets is a source. A decrease in reserves (e.g., due to a loss or buyback) is a use of funds, not a source.

Oct/Nov 2016

99. Which of the following best describes the main purpose of a Funds Flow Statement?
(A) To present the precise and verified cash and cash equivalents balance at the period's end.
(B) To provide a complete listing of all cash transactions in the exact chronological order they occurred.
(C) To determine the changes in working capital and analyze the long-term financial strategy.
(D) To ensure the company complies with all the mandatory reporting requirements of Ind AS-7.

Ans :

(C) To determine the changes in working capital and analyze the long-term financial strategy.
The Funds Flow Statement is a broader analytical tool compared to the cash flow statement. Its primary objectives are to explain the change in a company's net working capital over a period and to provide insights into how the company has financed its long-term investments and growth, revealing its overall financial strategy.

May/June 2020

100. When preparing a funds flow statement, if a company reports a net profit for the year, this amount is treated as:
(A) A source of funds
(B) A use of funds
(C) A short-term liability
(D) A non-fund item to be ignored

Ans :

(A) A source of funds
The net profit generated from operations (after adjusting for non-fund items like depreciation) represents a primary source of funds for the enterprise. These internally generated funds can then be used for various purposes like acquiring assets, repaying debt, or paying dividends. Therefore, net profit is a key component of the 'sources of funds'.

Oct/Nov 2019

101. Which of the following statements is incorrect regarding the preparation of a Funds Flow Statement?
(A) A decrease in assets represents a source of funds.
(B) An increase in liabilities represents a source of funds.
(C) A decrease in liabilities represents a source of funds.
(D) An increase in assets represents a use of funds.

Ans :

(C) A decrease in liabilities represents a source of funds.
A decrease in liabilities, such as the repayment of a loan, requires an outflow of funds from the company. This application of financial resources to settle an obligation is therefore treated as a use of funds, not a source. The other three statements correctly describe the principles of sources and uses in a funds flow analysis.

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Oct/Nov 2006

121. Consider the following statements about cash flow classification:

1. Interest paid can be classified as an operating activity.
2. Dividends received can be classified as an investing activity.
3. For a bank, making a loan to a customer is an investing activity.

Which of the above statements are correct?

(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(A) 1 and 2 only
Statement 1 is correct as interest paid is often classified under operating activities. Statement 2 is correct as dividends received are returns on an investment and can be classified as an investing activity. Statement 3 is incorrect; for a bank, making loans is a principal revenue-producing activity and is therefore classified as an operating activity.

May/June 2023

122. Which of the following would NOT be found in the 'Financing Activities' section of a cash flow statement?

(A) Increase in equity
(B) Sale of long-term assets
(C) Decrease in borrowings
(D) Payment of dividend

Ans :

(B) Sale of long-term assets
The sale of long-term assets is a disposal of an investment made by the company. The cash proceeds from such a sale are classified as a cash inflow from investing activities. All the other options—increase in equity, decrease in borrowings, and payment of dividend—are transactions with capital providers and are correctly classified under financing activities.

Oct/Nov 2024

123. The primary benefit of a cash flow statement is that it provides information to evaluate an entity's financial structure, including its:

(A) Market share and customer satisfaction
(B) Employee turnover and morale
(C) Liquidity and solvency
(D) Product quality and innovation

Ans :

(C) Liquidity and solvency
The cash flow statement is crucial for assessing an entity's financial health. It provides direct insight into liquidity (the ability to meet short-term obligations) and solvency (the ability to meet long-term obligations). By showing how a company generates and uses cash, it helps users judge its financial flexibility and overall stability.

May/June 2018

124. From a funds flow perspective, if a company issues debentures for cash, it results in:

(A) An increase in a liability and an increase in a current asset (cash).
(B) A long-term source of funds and a short-term use of funds.
(C) An increase in long-term borrowings (source) and an increase in cash.
(D) A long-term source of funds (increase in debentures).

Ans :

(D) A long-term source of funds (increase in debentures).
In a funds flow statement, the transaction is analyzed in terms of its net effect on funds. The issuance of long-term debentures increases the company's long-term borrowings. This increase in a long-term liability is classified as a long-term source of funds. The corresponding increase in cash is part of the overall change in working capital.

Oct/Nov 2025

125. The term 'funds' in a Funds Flow Statement most commonly refers to:

(A) Net working capital (Current Assets - Current Liabilities)
(B) Only the total of cash on hand and all designated cash equivalents.
(C) The total amount of equity attributable to the company's shareholders.
(D) The aggregate value of all assets, both current and non-current, owned by the entity.

Ans :

(A) Net working capital (Current Assets - Current Liabilities)
While the term 'funds' can be defined in various ways, in the most common usage of a Funds Flow

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contract must also be classified as investing activities.

Oct/Nov 2013

107. A company acquires a new building by issuing its own shares to the seller instead of paying cash. How is this transaction reported?

(A) Reported as both an investing cash inflow and a financing cash outflow in the statement.
(B) Reported solely as a cash outflow for investing activities within the cash flow statement.
(C) The transaction is completely ignored and omitted from all sections of the financial report.
(D) It is excluded from the cash flow statement but disclosed in the notes to the financial statements.

Ans :

(D) It is excluded from the cash flow statement but disclosed in the notes to the financial statements.
Non-cash investing and financing transactions are excluded from the body of the cash flow statement. Since no cash changed hands in this acquisition, it cannot be reported as a cash flow. However, it is a significant investing and financing activity that must be disclosed to users in the notes accompanying the financial statements.

May/June 2010

108. What is a primary reason for a banker to analyze a funds flow statement with a long-term/short-term classification?

(A) To detect potential financial indiscipline, such as using a 5-year loan to pay salaries.
(B) To independently calculate the company's net profit figure for the reporting period.
(C) To perform a verification of the final closing cash and cash equivalents balance.
(D) To ascertain the current market capitalization of the company based on its share price.

Ans :

(A) To detect potential financial indiscipline, such as using a 5-year loan to pay salaries.
Bankers use a classified funds flow format to check for the diversion of funds. Using long-term funds (like a 5-year loan intended for capital expenditure) for short-term uses (like paying salaries) is a serious financial mismatch and a red flag for lenders. The classified funds flow statement makes such diversions clearly visible.

Oct/Nov 2015

109. A company's fixed assets were ₹10,00,000 on both 31/3/21 and 31/3/22. Depreciation for the year was ₹85,000. Based on funds flow principles, what does this imply?

(A) No entry is needed as the net value is unchanged.
(B) A source of funds of ₹85,000 is shown.
(C) A source of ₹85,000 and a use of ₹85,000 are both shown.
(D) A use of funds of ₹85,000 is shown.

Ans :

(C) A source of ₹85,000 and a use of ₹85,000 are both shown.
Depreciation is a source of funds (as it's a non-fund expense added back to calculate funds from operations). The fact that the asset value did not decrease implies that new assets worth ₹85,000 must have been purchased to offset the depreciation charge. This purchase is a use of funds. Therefore, both a source and a use of ₹85,000 must be shown in the funds flow statement.

May/June 2009

110. Which of the following statements correctly represents a 'use of funds' in a funds flow statement?

(A) A decrease in short-term borrowings.
(B) An increase in long-term borrowings.
(C) A decrease in non-current assets.
(D) An increase in reserves.

Ans :

(A) A decrease in short-term borrowings.
A decrease in short-term borrowings signifies that the company has used its funds to repay its short-term lenders. This application of funds is classified as a use. Increases in borrowings or reserves are sources of funds, and a decrease in non-current assets is also a source of funds as it releases capital.

Oct/Nov 2022

111. Consider the following statements:
Statement I : A cash flow statement is mandatory and an integral part of financial statements.
Statement II : A funds flow statement is primarily used to understand the liquidity position of a business.

(A) Statement I is correct, but Statement II is incorrect.

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Oct/Nov 2021

93. According to Ind AS-7, which method of reporting operating cash flows adjusts profit or loss for the effects of non-cash transactions?
(A) The direct method
(B) The gross method
(C) The indirect method
(D) The equity method

Ans :

(C) The indirect method
The indirect method is a reconciliation approach. It begins with the accrual-based profit or loss figure and makes several adjustments to arrive at the net cash flow from operations. These adjustments include reversing non-cash items like depreciation, accounting for deferrals and accruals, and removing the effects of any investing or financing transactions included in net profit.

May/June 2011

94. Given that financing activities help predict claims on future cash flows, why would an analyst pay close attention to a large cash inflow from the issuance of bonds?
(A) To make a detailed assessment of the company's inherent ability to generate future sales revenue.
(B) To calculate the precise amount of depreciation that will be charged in the next accounting period.
(C) To perform an evaluation of the company's total expenditure on acquiring new fixed assets.
(D) To predict future cash outflows for interest payments and principal repayment.

Ans :

(D) To predict future cash outflows for interest payments and principal repayment.
Financing activities are useful for predicting claims on future cash flows by providers of capital. Issuing bonds creates a liability that requires future cash outflows for periodic interest payments and the eventual repayment of the principal. An analyst sees this inflow as an indicator of future fixed cash commitments to providers of debt capital.

Oct/Nov 2007

95. An entity discloses its components of cash and cash equivalents and presents a reconciliation of these amounts with the equivalent items reported in the balance sheet. What is the primary purpose of this reconciliation?
(A) To link the cash flow statement to the balance sheet, ensuring consistency.
(B) To prove the mathematical accuracy of the profit calculation.
(C) To calculate the amount of income tax payable for the period.
(D) To show the impact of non-cash transactions on the entity's assets.

Ans :

(A) To link the cash flow statement to the balance sheet, ensuring consistency.
This reconciliation is a mandatory disclosure that bridges the gap between two key financial statements. It confirms that the 'cash and cash equivalents' figure used as the opening and closing balance in the cash flow statement corresponds directly to the relevant line items (e.g., Cash in Hand, Bank Balances) presented on the balance sheet.

May/June 2005

96. Match List-I (Cash Flow Statement Feature) with List-II (Funds Flow Statement Feature).
List-I
P. Focuses on cash and cash equivalents
Q. Segregates activities into three categories
R. Mandatory part of financial statements
S. Uses cash system of accounting
List-II
1. Not a mandatory requirement
2. Focuses on changes in working capital
3. Uses accrual system of accounting
4. No segregation of activities is required
(A) P-2, Q-4, R-1, S-3
(B) P-1, Q-2, R-3, S-4
(C) P-2, Q-3, R-4, S-1
(D) P-4, Q-1, R-2, S-3

Ans :

(A) P-2, Q-4, R-1, S-3
This question matches contrasting features. P(Cash focus) contrasts with 2(Working Capital focus). Q(Segregation) contrasts with 4(No Segregation). R(Mandatory) contrasts with 1(Not Mandatory). S(Cash system) contrasts with 3(Accrual system).

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May/June 2012

116. A company's balance sheets show that 'Reserves' decreased from ₹2,00,000 to ₹1,50,000. During the year, the company earned a net profit of ₹80,000. What is the amount of dividend paid during the year?
(A) ₹50,000
(B) ₹1,30,000
(C) ₹80,000
(D) ₹30,000

Ans :

(B) ₹1,30,000
The opening reserve was ₹2,00,000. Adding the net profit of ₹80,000 would have brought the balance to ₹2,80,000. However, the closing balance is only ₹1,50,000. The difference (₹ 2,80,000 - ₹ 1,50,000 = ₹ 1,30,000) must have been paid out as dividends, which is a use of funds and reduces the reserves.

Oct/Nov 2008

117. Which of the following activities is correctly paired with its cash flow classification for a manufacturing firm?
(A) Payment of dividends - Operating activity
(B) Purchase of raw materials - Investing activity
(C) Sale of old machinery - Investing activity
(D) Issuance of debentures - Operating activity

Ans :

(C) Sale of old machinery - Investing activity
The sale of old machinery is the disposal of a long-term asset, and the cash proceeds are correctly classified as an inflow from investing activities. Payment of dividends is a financing activity. Purchase of raw materials is an operating activity. Issuance of debentures is a financing activity.

May/June 2007

118. What is the fundamental principle behind identifying sources and applications of funds by comparing two balance sheets?
(A) The accounting equation, where any change on one side must be matched by a change on the other, reflecting a source and a use.
(B) The fundamental rule that a balance sheet's total assets must equal its liabilities plus equity.
(C) The principle that every single change in any balance sheet item must result from a fund movement.
(D) The assumption that net profit is the sole and only genuine source of funds for an enterprise.

Ans :

(A) The accounting equation, where any change on one side must be matched by a change on the other, reflecting a source and a use.
The preparation of a funds flow statement is based on the logic of the accounting equation. A transaction causes changes in balance sheet items. For example, buying an asset (use) with a loan (source) changes both sides. Analyzing the net changes between two balance sheets reveals the aggregate sources and uses over the period.

Oct/Nov 2014

119. A decrease in equity in a funds flow statement is classified as a:
(A) Long-term source
(B) Short-term source
(C) Long-term use
(D) Short-term use

Ans :

(C) Long-term use
A decrease in equity, for example through a share buy-back or a withdrawal of capital, represents an outflow of funds from the company back to its owners. This application of funds reduces the long-term capital base of the company and is therefore classified as a long-term use of funds.

May/June 2016

120. When preparing a cash flow statement using the indirect method, an increase in 'Other items of current assets' is:
(A) Subtracted from operating income
(B) Added to operating income
(C) Shown as an investing outflow
(D) Shown as a financing outflow

Ans :

(A) Subtracted from operating income
An increase in a current asset (other than cash) signifies that cash has been used or tied up. For example, an increase in prepaid expenses means cash was paid out in advance of the expense being recognized. This use of cash reduces the net cash generated from operations, so it is subtracted from operating income.

NODIA

May/June 2013

102. If a company's Share Capital increased from ₹5,00,000 to ₹7,00,000, how would this change be classified in a funds flow statement?
(A) As an application of funds
(B) As a source of funds
(C) As a non-fund transaction
(D) As a decrease in assets

Ans :

(B) As a source of funds
An increase in liabilities, which includes shareholder's equity, is a source of funds. An increase in share capital signifies that the company has received additional funds from its owners by issuing new shares. Therefore, this ₹2,00,000 increase would be classified as a source of funds in the statement.

Oct/Nov 2010

103. If a company's Long-Term Debt decreased from ₹3,00,000 to ₹2,50,000, how would this change be classified in a funds flow statement?
(A) As an application of funds
(B) As a source of funds
(C) As an increase in assets
(D) As a non-fund item

Ans :

(A) As an application of funds
A decrease in liabilities is considered an application of funds. A reduction in long-term debt implies that the company has used its funds to repay a portion of its borrowings. This outflow of resources to settle a liability is therefore an application, or use, of funds.

May/June 2025

104. What is the final step in constructing the main body of a cash flow statement, after determining the flows for the three main activity groups?
(A) The classification of every single transaction into either a source or a use of funds.
(B) The process of starting with net profit and then adding back the non-cash depreciation charge.
(C) The detailed reconciliation of the book cash balance with the official bank statement balance.
(D) Summing the net cash flows from operating, investing, and financing activities to find the total net cash flow.

Ans :

(D) Summing the net cash flows from operating, investing, and financing activities to find the total net cash flow.
The process of preparing a cash flow statement involves first calculating the net cash flow for each of the three categories (operating, investing, and financing). The final step is to aggregate these three amounts. The sum of these individual net flows provides the overall net cash flow for the enterprise during the specified reporting period.

Oct/Nov 2009

105. A mutual fund company buys shares worth ₹1 crore for its trading portfolio. How should this transaction be classified in its cash flow statement?
(A) As an operating cash outflow
(B) As an investing cash outflow
(C) As a financing cash outflow
(D) As a non-cash transaction

Ans :

(A) As an operating cash outflow
When securities are held for dealing or trading purposes, they are treated like inventory. For a mutual fund company, buying and selling securities is its principal revenue-producing activity. Therefore, the cash outflow for purchasing these trading securities is classified as an operating activity, not an investing one.

May/June 2006

106. A company enters into a forward contract to hedge against currency fluctuations on a large machine it is importing. The purchase of the machine is an investing activity. How should a payment made on the forward contract be classified?
(A) As an operating activity
(B) As an investing activity
(C) As a financing activity
(D) As a cash equivalent

Ans :

(B) As an investing activity
The cash flow of a hedging contract is classified in the same manner as the cash flow of the item being hedged. In this case, the forward contract is hedging a machine import, which is an investing activity (acquisition of a long-term asset). Therefore, the cash flows related to the forward

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Statement, it refers to net working capital. The statement is therefore often called a 'Statement of Changes in Working Capital,' as its primary purpose is to explain the net increase or decrease in this figure.

May/June 2015

126. Which of the following is an example of a non-cash investing and financing activity?
(A) The act of distributing profits to shareholders in the form of cash dividends.
(B) A routine operational transaction involving the sale of inventory on credit terms.
(C) The repayment of an outstanding bank loan principal using the company's cash reserves.
(D) Purchasing machinery and paying for it with a long-term note payable.

Ans :

(D) Purchasing machinery and paying for it with a long-term note payable.
This transaction involves a significant investing activity (acquiring machinery) and a significant financing activity (incurring long-term debt). However, no cash is exchanged at the time of the transaction. As per accounting standards, such non-cash activities are excluded from the cash flow statement but must be disclosed in the notes to provide complete information.

Oct/Nov 2018

127. Identify the correct statement.
(A) Cash flow from operating activities is always positive for a healthy company.
(B) A negative cash flow from investing activities is always a bad sign.
(C) A positive cash flow from financing activities may indicate reliance on external debt or equity.
(D) The sum of cash flows from all three activities must equal the company's net profit.

Ans :

(C) A positive cash flow from financing activities may indicate reliance on external debt or equity.
A positive cash flow from financing activities means the company raised more money from owners and lenders than it paid back. This can be a strategic move for expansion, but it can also indicate that the company's operations are not generating enough cash, forcing it to rely on external funding sources like new loans or share issues.

May/June 2021

128. An increase in short-term borrowings is a _____, while a decrease in short-term borrowings is a _____.
(A) Short-term source; Short-term use
(B) Long-term source; Long-term use
(C) Short-term use; Short-term source
(D) Long-term use; Long-term source

Ans :

(A) Short-term source; Short-term use
An increase in short-term borrowings (like a bank overdraft) provides the company with immediate funds, making it a short-term source. Conversely, a decrease in these borrowings means the company has used its funds to repay the debt, which constitutes a short-term use of funds. This directly impacts the short-term financing structure.

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Oct/Nov 2005

129. The main objective of a business enterprise is to earn profit. However, it is also important to ensure its cash flow is not negative for a long period because:
(A) A period of negative cash flow will invariably cause a decrease in the company's share price.
(B) Sustained negative cash flow is considered an illegal practice under current accounting standards.
(C) The firm will eventually run out of cash to purchase commodities and sustain operations.
(D) It is a definitive indicator that the company has ceased all investment in long-term assets.

Ans :

(C) The firm will eventually run out of cash to purchase commodities and sustain operations.
Even a profitable company cannot survive without cash. A persistently negative cash flow will deplete the company's liquid resources. This will ultimately lead to a situation where the firm cannot pay its suppliers, employees, or other creditors, making it impossible to purchase necessary goods or services and forcing it to cease operations.

May/June 2014

130. A firm purchases a machine for ₹1,00,000 by paying ₹20,000 in cash and issuing shares for the

remaining ₹80,000. How would this be reflected in the Cash Flow Statement?

(A) An investing outflow of ₹20,000.
(B) An investing outflow of ₹1,00,000.
(C) An investing outflow of ₹20,000 and a financing inflow of ₹80,000.
(D) An investing outflow of ₹1,00,000 and a financing inflow of ₹80,000.

Ans :

(A) An investing outflow of ₹20,000.
The statement of cash flows only reports transactions involving cash and cash equivalents. The only cash part of this transaction was the ₹20,000 payment for the machine, which is an investing outflow. The ₹80,000 share issuance is a significant non-cash investing and financing activity that would be disclosed separately in the notes.

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CHAPTER 17

Final Accounts of Banking Companies

May/June 2016

1. According to the Banking Regulation Act of 1949, which of the following is NOT a primary objective of its enactment?
(A) To regulate the various aspects of the banking business in India
(B) To facilitate the nationalisation of all private sector banks through a single legislative act
(C) To protect the financial interests and build the confidence of depositors
(D) To provide a comprehensive legal framework for all banking companies

Ans :

(B) To facilitate the nationalisation of all private sector banks through a single legislative act
The Banking Regulation Act of 1949 was enacted to regulate the banking business and safeguard the interests of the large number of depositors. While it provides the legal framework for banking, its primary objectives did not include the facilitation of nationalising all private sector banks, which occurred through separate legislative actions much later.

Oct/Nov 2025

2. The Banking Regulation Act of 1949 came into force on which date?
(A) 16th March, 1949
(B) 15th August, 1947
(C) 26th January, 1950
(D) 1st April, 1949

Ans :

(A) 16th March, 1949
The Banking Regulation Act of 1949 was a crucial piece of legislation designed to regulate the banking sector in India. It officially came into force on 16th March, 1949, addressing the long-felt need to structure the banking business and protect the interests of depositors across the country, fostering a more stable economic environment.

May/June 2023

3. Which of the following is NOT listed as a major institution carrying on banking business in India?
(A) Small Finance Banks
(B) Co-operative banks
(C) Non-Banking Financial Companies (NBFCs)
(D) Payments Banks

Ans :

(C) Non-Banking Financial Companies (NBFCs)
The text identifies several major institutions in the Indian banking system, including Nationalised banks, State Bank of India, Foreign banks, Co-operative banks, Regional Rural banks, Private sector banks, Small Finance Banks, and Payments Banks. Non-Banking Financial Companies (NBFCs) are financial institutions but are distinct from banking companies as defined in this context.

Oct/Nov 2010

4. As per Section 5 of the Banking Regulation Act, "banking" is defined as accepting deposits of money from the public for which primary purpose?
(A) For the purpose of safe-keeping and secure custody only
(B) For the purpose of providing payment and settlement services
(C) For the purpose of facilitating various government transactions
(D) For the purpose of lending or investment

Ans :

(D) For the purpose of lending or investment
Section 5 of the Banking Regulation Act defines banking as the activity of accepting deposits of money from the public. The core purpose specified for accepting these deposits is for lending them out to borrowers or for making investments. The deposits are repayable on demand or otherwise and can be withdrawn by various means like cheque or draft.

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For public transparency, banks are required to publish their financial results. Rule 15 of the Banking Regulating (Companies) Rules, 1949, prescribes that the audited accounts and the accompanying auditor's report must be published in a newspaper that circulates in the area of the bank's principal office. This publication must occur within six months from the period's end.

May/June 2010

15. What system of accounting do banks, like most other large-sized institutions, typically follow?
(A) Mercantile system
(B) Cash system
(C) Hybrid system
(D) Single-entry system

Ans :

(A) Mercantile system
Banks generally adhere to the mercantile system of accounting, also known as the accrual basis of accounting. Under this system, revenues and expenses are recognized when they are earned or incurred, regardless of when the cash is actually received or paid. This provides a more accurate picture of the bank's financial performance and position during a period.

Oct/Nov 2024

16. In the accounting system of banks, which of the following is given relatively lesser emphasis compared to other enterprises?
(A) Customer ledgers and their real-time accuracy
(B) Books of prime entry like cash books or journals
(C) The general ledger for control and consolidation
(D) Subsidiary ledgers for loans and deposits

Ans :

(B) Books of prime entry like cash books or journals
While most enterprises focus heavily on keeping books of prime entry (like cash books and journals) up-to-date, banks place a stronger emphasis on the accuracy and real-time updating of ledger accounts, especially those of customers. The system often relies on direct posting from vouchers, placing relatively less emphasis on traditional, detailed books of prime entry.

May/June 2017

17. The accounting procedure where transactions are entered directly into ledgers from documents like pay-in slips and withdrawal slips is known as the:
(A) Double-entry system
(B) Slip system of posting
(C) Journal-first system
(D) Day book system

Ans :

(B) Slip system of posting
Banks utilize a method called the 'Slip System' of posting to ensure customer accounts are updated promptly. In this system, transactions are first entered into the customer accounts directly from source documents like pay-in slips and cheques. Subsequently, Day Books are written up, which is a reversal of the process in many other businesses.

Oct/Nov 2005

18. According to Section 2(3) of the Bankers' Books Evidence Act, which of the following is included in the definition of 'Bankers' Books'?
(A) Ledgers, day book, cash books, account books, and all other books used in ordinary business
(B) Only ledgers and cash books as primary records of financial transactions
(C) Only day books and account books used for daily reconciliation purposes
(D) Only electronic records and server logs stored in a digital format

Ans :

(A) Ledgers, day book, cash books, account books, and all other books used in ordinary business
The Bankers' Books Evidence Act provides a broad definition under Section 2(3). 'Bankers' Books' are not limited to just a few specific books but include ledgers, day books, cash books, account books, and importantly, all other books that are used in the ordinary course of a bank's business, making the definition comprehensive and inclusive.

May/June 2020

19. Which of the following is NOT a type of ledger book typically maintained by a bank?
(A) Current Accounts Ledger
(B) FD Accounts Ledger
(C) Employee Attendance Ledger
(D) Investment Ledger

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who is responsible for the business conducted here.

Oct/Nov 2007

10. According to Section 30 of the Banking Regulation Act, what is a mandatory prerequisite for a banking company before appointing, reappointing, or removing an auditor?
(A) Prior approval of the Reserve Bank of India
(B) Approval from the Ministry of Finance, Government of India
(C) A special resolution passed by a two-thirds majority of shareholders
(D) Written consent from the Institute of Chartered Accountants of India

Ans :

(A) Prior approval of the Reserve Bank of India
Section 30 of the Act imposes a significant regulatory check on the audit process of banks. To ensure auditor independence and quality, every banking company is required to obtain the prior approval of the Reserve Bank of India (RBI) before it can appoint, reappoint, or remove any auditor. This gives the RBI oversight on audit appointments.

May/June 2025

11. As per Section 31 of the Banking Regulation Act, within what timeframe must a banking company submit its audited financial statements to the Reserve Bank of India?
(A) Within one month from the end of the period
(B) Within six months from the end of the period
(C) Within nine months from the end of the period
(D) Within three months from the end of the period

Ans :

(D) Within three months from the end of the period
Section 31 mandates the timely submission of financial reports to the regulator. A banking company must submit three copies of its balance sheet, profit and loss account, and the auditor's report to the RBI. This submission must be made within three months from the end of the accounting period to which the statements relate.

Oct/Nov 2019

12. The Reserve Bank of India has the authority to extend the submission period for financial statements by a banking company for a further period of up to how many months?
(A) One month
(B) Three months
(C) Two months
(D) Six months

NODIA

Ans :

(B) Three months
While the standard deadline for submitting audited accounts to the RBI is three months from the financial year-end, Section 31 provides some flexibility. The Reserve Bank of India can, if it deems necessary, grant an extension. This extension for submission can be for a further period not exceeding three months, making the maximum possible timeline six months.

May/June 2009

13. Which section of the Banking Regulation Act requires a banking company to furnish copies of its annual accounts to the Registrar of Companies?
(A) Section 29
(B) Section 30
(C) Section 32
(D) Section 31

Ans :

(C) Section 32
In addition to submitting accounts to the RBI, banking companies have a dual reporting obligation. Section 32 of the Banking Regulation Act requires a banking company to furnish three copies of its annual accounts and the auditor's report to the Registrar of Companies (RoC). This must be done at the same time it furnishes these documents to the RBI.

Oct/Nov 2011

14. According to Rule 15 of the Banking Regulating (Companies) Rules, 1949, within what period from the end of the financial year must a bank publish its accounts and auditor's report in a newspaper?
(A) Three months
(B) Four months
(C) Nine months
(D) Six months

Ans :

(D) Six months

in a completely separate ledger from current deposit accounts

Ans :

(C) Each control account in the general ledger is supported by one or more subsidiary ledgers
The accounting system uses a control account structure for efficiency and accuracy. Each control account in the general ledger, such as 'Total Deposits' or 'Total Loans', is supported by a corresponding subsidiary ledger (or multiple ledgers). These subsidiary ledgers contain the detailed individual accounts of each customer, and their total balance must match the control account.

Oct/Nov 2008

24. For which of the following are separate registers typically maintained by a bank, rather than allotting separate folios to each customer?
(A) Current accounts
(B) Cash credit accounts
(C) Savings accounts
(D) Term deposits

Ans :

(D) Term deposits
While individual folios are allotted for transactional accounts like savings and current accounts, banks generally do not allot separate folios for each term deposit customer. Instead, they maintain registers for term deposits, often sectionalized by the period of deposit or the interest rate, to record the necessary particulars of these instruments.

May/June 2006

25. What is the primary purpose of maintaining party-wise details in a separate ledger form for bills purchased or discounted?
(A) To ensure that the sanctioned limits of parties are not exceeded
(B) To calculate the total income earned from discounting activities
(C) To segregate the bills based on their respective maturity dates
(D) To track the geographical location of the drawees on the bills

Ans :

(A) To ensure that the sanctioned limits of parties are not exceeded
When a bank purchases or discounts bills for a customer, it is extending a form of credit. To manage the credit risk associated with each party, the bank maintains party-wise details in a ledger. This practice is crucial to monitor the total exposure to a single party and ensure that it remains within the pre-approved sanctioned limits.

Oct/Nov 2017

26. In the context of a bank's accounting, what happens when a bill sent for collection is finally realised?
(A) A new contra entry is created to reflect the income earned from the collection service
(B) The original contra entry made at the time of receipt is reversed
(C) The bill is moved from the Bills for Collection Register to the Bills Purchased Register
(D) A suspense account is credited with the amount collected pending instruction from the customer

Ans :

(B) The original contra entry made at the time of receipt is reversed
When a bank accepts a bill for collection, it is an agency service, and a contra entry is passed to record the asset (Bill for Collection) and liability (to the customer). Upon successful collection of the amount, this original entry is reversed, as the bill is no longer held and the liability to the customer is settled by crediting their account.

May/June 2008

27. The account used to channelise funds for frequent transactions between a bank's branches and its head office is known as a:
(A) Suspense account
(B) Vostro account
(C) Nodal account or Inter-office account
(D) Contra account

Ans :

(C) Nodal account or Inter-office account
Transactions between branches, or between a branch and the head office, are settled through a specific mechanism. This involves a nodal account, which might be called the Head Office Account or Inter-office Account. This account is crucial for consolidating transactions and is closely monitored to prevent fraud and ensure timely reconciliation of entries.

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Ans :

(C) Employee Attendance Ledger
Banks maintain several specialized ledger books to manage their core operations. These include ledgers for Current Accounts, FD Accounts, RD Accounts, Loans, Investments, and Bills discounted and purchased. An Employee Attendance Ledger, while important for HR, is not considered a principal book of account for financial transaction recording in this context.

Oct/Nov 2015

20. Which of the following is a book maintained by a bank for non-financial record-keeping that supports account entries?
(A) Safe deposit vault Register
(B) General Ledger
(C) Profit and Loss Ledger
(D) Current Accounts Ledger

Ans :

(A) Safe deposit vault Register
Banks maintain several 'Other Books' or registers that are not part of the core double-entry accounting system but are crucial for record-keeping and control. The Safe deposit vault Register tracks the usage and details of safe deposit lockers, supporting fee income entries and managing operational risk, unlike the General Ledger which is a core accounting book.

May/June 2013

21. In a bank's General Ledger, what is the function of 'contra accounts'?
(A) To specifically record transactions, such as losses or write-offs, that directly decrease the bank's net worth
(B) To act as a clearing account used to temporarily offset and correct errors made in individual customer ledgers
(C) To consolidate and record all transactions involving the purchase and sale of foreign currency for reporting purposes
(D) To track off-balance sheet items, such as guarantees given, that represent contingent liabilities

Ans :

(D) To track off-balance sheet items, such as guarantees given, that represent contingent liabilities
Contra accounts are maintained in the General Ledger to track and control transactions that represent contingent liabilities or agency services. These items, such as letters of credit opened, bills received for collection, or guarantees given, do not immediately impact the bank's primary assets and liabilities but need to be monitored closely.

Oct/Nov 2021

22. Which statement correctly describes the relationship between the Profit and Loss Ledger and the published Profit and Loss Account of a bank?
(A) They are required by regulation to be identical in every detail to ensure consistency between internal and external reports
(B) The P&L Ledger uses more granular account heads for internal control, which are aggregated for the published P&L Account
(C) The Profit and Loss Ledger is a high-level summary created after the more detailed published Profit and Loss Account is finalized
(D) The published P&L Account is prepared directly from transaction vouchers, while the P&L Ledger is a secondary book prepared from the trial balance

Ans :

(B) The P&L Ledger uses more granular account heads for internal control, which are aggregated for the published P&L Account
For internal managerial control, the Profit and Loss Ledger maintains a high level of detail. For example, it has separate accounts for basic salary, dearness allowance, etc. In the published financial statements, these detailed heads are grouped together into broader categories like 'Payments to and Provisions for Employees' for external reporting purposes.

May/June 2024

23. In the context of a bank's subsidiary books, which statement is true regarding personal ledgers?
(A) A single, comprehensive personal ledger contains all customer accounts, including both deposits and loans
(B) Subsidiary ledgers are maintained by banks only for high-value deposit accounts exceeding a certain threshold
(C) Each control account in the general ledger is supported by one or more subsidiary ledgers
(D) Overdraft accounts are always maintained

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the amount brought in as start-up capital, as stipulated by the Reserve Bank of India. Additionally, it includes the amount of deposit that the foreign bank is required to maintain with the RBI under Section 11(2) of the Banking Regulation Act.

May/June 2022

33. Which of the following is NOT a component of Schedule 2 'Reserves and Surplus'?
(A) Statutory reserves
(B) Share premium
(C) Unclaimed dividends
(D) Investment reserve

Ans :

(C) Unclaimed dividends
Schedule 2 'Reserves and Surplus' includes various reserves created by the bank. Common components are statutory reserves, capital reserves, share premium, investment reserve, and the balance in the profit and loss account. Unclaimed dividends, however, are a liability to shareholders and are typically shown under Schedule 5 'Other Liabilities and Provisions'.

Oct/Nov 2023

34. In Schedule 3 'Deposits' of a bank's balance sheet, how are matured term deposits classified?
(A) As Term deposits
(B) As Other Liabilities
(C) As Borrowings
(D) As Demand deposits

Ans :

(D) As Demand deposits
Once a term deposit or a cash certificate matures, its nature changes. It is no longer a time liability but becomes payable to the customer on demand. Therefore, for the purpose of classification in Schedule 3, matured time deposits are correctly treated and included under the category of 'Demand deposits' along with other on-demand liabilities.

May/June 2018

35. Identify the correct statement regarding Schedule 4 'Borrowings'.
(A) Money at call or short notice taken by the bank is shown under this head.
(B) This schedule primarily includes deposits accepted from the general public.
(C) It specifically excludes any borrowings from the Reserve Bank of India.
(D) Inter-office transactions and adjustments are shown as borrowings.

Ans :

(A) Money at call or short notice taken by the bank is shown under this head.
Schedule 4 'Borrowings' includes funds raised by the bank from sources other than public deposits. This encompasses borrowings from the RBI, other banks, and financial institutions. Importantly, funds taken by the bank from the inter-bank market as 'money at call or short notice' are also classified as borrowings under this schedule.

Oct/Nov 2018

36. Under which schedule of the Balance Sheet would a bank show 'Bills Payable'?
(A) Schedule 3: Deposits
(B) Schedule 5: Other Liabilities and Provisions
(C) Schedule 4: Borrowings
(D) Schedule 9: Advances

Ans :

(B) Schedule 5: Other Liabilities and Provisions
'Bills Payable' represents the bank's obligation for instruments like demand drafts, pay orders, and telegraphic transfers that have been issued but not yet presented for payment. This outstanding liability is not a deposit or a borrowing but is correctly classified under Schedule 5 'Other Liabilities and Provisions' in the bank's balance sheet.

May/June 2007

37. 'Balances with Banks and Money at Call and Short Notice' are detailed in which schedule?
(A) Schedule 6
(B) Schedule 8
(C) Schedule 9
(D) Schedule 7

Ans :

(D) Schedule 7
Schedule 7 of a bank's balance sheet details its liquid assets placed with other financial institutions. This schedule, titled 'Balances with Banks and Money at Call and Short Notice', includes funds in current and deposit accounts with other banks, as well as short-term funds lent in the inter-bank money market, both in India and outside India.

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Oct/Nov 2013

28. What is a peculiar feature of a bank's internal accounting system regarding its branches' funds?
(A) Branches notionally have no funds of their own and all funds are deemed to be with the head office
(B) Each branch is required to manage its own capital and reserves independently from the head office
(C) All profits generated by a branch are retained at the branch level for local reinvestment and expansion
(D) Branches are permitted to lend funds directly to each other at market-driven, arm's-length interest rates

Ans :

(A) Branches notionally have no funds of their own and all funds are deemed to be with the head office
A unique aspect of bank accounting is the notional treatment of branch funds. All deposits a branch accepts are deemed to be passed on to the head office, and all loans it makes are considered to be from funds provided by the head office. The head office then charges or pays interest to the branch accordingly, which gets offset during consolidation.

May/June 2015

29. In the prescribed format of a bank's Balance Sheet (Form A), which schedule details the 'Reserves and Surplus'?
(A) Schedule 1
(B) Schedule 3
(C) Schedule 2
(D) Schedule 5

Ans :

(C) Schedule 2
According to the Third Schedule of the Banking Regulation Act, the Balance Sheet (Form A) is supported by several detailed schedules. Schedule 2 is specifically designated for providing the breakdown of a bank's 'Reserves and Surplus', which includes items like statutory reserves, capital reserves, share premium, and the balance of profit and loss account.

Oct/Nov 2012

30. Which of the following items would be found under Schedule 9 of a bank's Balance Sheet?
(A) Advances
(B) Investments
(C) Borrowings
(D) Fixed Assets

Ans :

(A) Advances
Schedule 9 of the Balance Sheet (Form A) provides a detailed classification of the bank's loan portfolio. This schedule, titled 'Advances', includes categories such as bills purchased and discounted, cash credits, overdrafts, and term loans. It is a critical component of the asset side of the bank's balance sheet, representing its primary earning assets.

May/June 2011

31. Contingent Liabilities of a banking company are disclosed in which schedule of the Balance Sheet?
(A) Schedule 5
(B) Schedule 11
(C) They are shown as a footnote only and not in a schedule
(D) Schedule 12

Ans :

(D) Schedule 12
Contingent Liabilities represent potential obligations that may arise depending on the outcome of a future event. For a bank, these include items like guarantees, acceptances, and letters of credit. As per the prescribed format, these items are not part of the main balance sheet total but are disclosed separately in detail under Schedule 12.

Oct/Nov 2020

32. For a bank incorporated outside India, what does Schedule 1 'Capital' primarily represent?
(A) The total global capital of the parent bank as reported in its home country
(B) Start-up capital prescribed by RBI and deposits kept with RBI under Section 11(2)
(C) The total market value of all assets held in its Indian branches
(D) The authorized share capital specifically allocated for its Indian operations

Ans :

(B) Start-up capital prescribed by RBI and deposits kept with RBI under Section 11(2)
For foreign banks operating in India, Schedule 1 'Capital' has a specific meaning. It includes

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deposits

Ans :

(B) Guarantees given on behalf of constituents
A contingent liability is a potential obligation. When a bank issues a guarantee on behalf of a customer, it undertakes to pay a third party if the customer defaults. This creates a potential liability for the bank, which is contingent upon the customer's failure to perform. Such guarantees are therefore disclosed under Schedule 12 'Contingent Liabilities'.

May/June 2016

43. The requirement for banks to create a Statutory Reserve under Section 17 of the Banking Regulation Act must be disclosed under which schedule?
(A) Schedule 1: Capital
(B) Schedule 5: Other Liabilities and Provisions
(C) Schedule 2: Reserves and Surplus
(D) Schedule 12: Contingent Liabilities

Ans :

(C) Schedule 2: Reserves and Surplus
The statutory reserve, created by transferring a portion of the annual profit as mandated by the Banking Regulation Act, is a part of the bank's owned funds. It must be separately and clearly disclosed within Schedule 2 'Reserves and Surplus'. This distinguishes it from other reserves and highlights compliance with the statutory requirement.

Oct/Nov 2025

44. What is the correct treatment for 'Surplus on revaluation' of assets in a bank's financial statements?
(A) It should be treated as a revenue reserve and can be used to declare dividends
(B) It should be credited directly to the Profit and Loss account as other income
(C) It should be shown as a deduction from the value of the revalued asset
(D) It should be treated as a capital reserve and is not available for distribution as profit

Ans :

(D) It should be treated as a capital reserve and is not available for distribution as profit
A surplus arising from the revaluation of a bank's fixed assets is an unrealized gain. Accounting principles dictate that such surpluses should not be considered free for distribution through the profit and loss account. Instead, they must be treated as a capital reserve and disclosed under Schedule 2 'Reserves and Surplus'.

May/June 2023

45. RBI has advised banks to create an 'Investment Fluctuation Reserve' with effect from the year 2018-19. What is its primary purpose?
(A) To build up adequate reserves to protect against an increase in yields in the future
(B) To create a fund for the acquisition of new securities in the trading portfolio
(C) To provide for annual depreciation on fixed assets, particularly on revalued properties
(D) To meet recurring expenses related to investment management services and custodian fees

Ans :

(A) To build up adequate reserves to protect against an increase in yields in the future
The Investment Fluctuation Reserve (IFR) is a prudential measure. It is created to build a cushion against potential future losses on the investment portfolio. Specifically, an increase in market interest rates (yields) leads to a decrease in the market value of fixed-income securities, and the IFR helps absorb such mark-to-market losses.

Oct/Nov 2010

46. Which of the following is included under 'Demand Deposits' in Schedule 3?
(A) A recurring deposit account with six months remaining until maturity
(B) Credit balance in an overdraft account
(C) A Foreign Currency Non-Resident (FCNR) account held for a fixed term
(D) Annuity deposits that have not yet matured

Ans :

(B) Credit balance in an overdraft account
Demand deposits are liabilities payable on demand. While overdrafts are typically debit balances (advances), any credit balance in an overdraft or cash credit account represents funds deposited by the customer that are repayable on demand. Therefore, such credit balances are correctly classified as demand deposits under Schedule 3, 'From others'.

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Oct/Nov 2009

38. A bank's investments in government securities, shares, and debentures are presented under which schedule?
(A) Schedule 8
(B) Schedule 7
(C) Schedule 9
(D) Schedule 11

Ans :

(A) Schedule 8
Schedule 8, titled 'Investments', is where a bank discloses its portfolio of securities. This schedule provides a breakdown of investments in various categories, including government securities, other approved securities, shares, debentures and bonds, and investments in subsidiaries or joint ventures. It is a key asset category for the bank, generating interest and dividend income.

May/June 2012

39. In Schedule 9 'Advances', which of the following is NOT one of the primary classifications under section 'A'?
(A) Bills purchased and discounted
(B) Cash credits, overdrafts and loans repayable on demand
(C) Unsecured advances
(D) Term loans

Ans :

(C) Unsecured advances
Schedule 9 'Advances' classifies the loan portfolio by type, security, and sector. Section 'A' classifies advances by their nature. The three main categories listed are (i) Bills purchased and discounted, (ii) Cash credits, overdrafts and loans repayable on demand, and (iii) Term loans. 'Unsecured advances' is a classification based on security (Section 'B'), not type.

Oct/Nov 2014

40. Under Schedule 10 'Fixed Assets', which of the following is a required disclosure for premises and other fixed assets?
(A) A full reconciliation showing opening cost, additions, deductions, and cumulative depreciation
(B) Only the final net book value at year-end, explicitly prohibiting any reconciliation of opening and closing balances
(C) The current market value as determined by an independent, RBI-approved valuer, which must be updated annually for all assets
(D) The projected replacement cost of the assets in the current market, less the total accumulated depreciation charged over their life

Ans :

(A) A full reconciliation showing opening cost, additions, deductions, and cumulative depreciation
Schedule 10 requires a detailed reconciliation of the movement in fixed assets during the year. For items like premises and other fixed assets, the bank must disclose the cost as on the first day of the financial year, any additions and deductions during the year, and the cumulative depreciation charged to date, thereby arriving at the closing written-down value.

May/June 2021

41. Which of the following items is classified under Schedule 11 'Other Assets'?
(A) Gold held as an investment for trading or hedging purposes
(B) Term loans granted to various corporate clients
(C) Balances maintained with the Reserve Bank of India
(D) Non-banking assets acquired in satisfaction of claims

Ans :

(D) Non-banking assets acquired in satisfaction of claims
Schedule 11 'Other Assets' is a residual category for assets not classified elsewhere. It includes items like inter-office adjustments (net debit), interest accrued on investments, and non-banking assets. These are immovable or tangible properties that the bank has acquired in the process of recovering a loan, which it must dispose of within a specified period.

Oct/Nov 2006

42. Which of the following represents a contingent liability for a bank and is shown under Schedule 12?
(A) Fixed deposits that are maturing in the next financial year
(B) Guarantees given on behalf of constituents
(C) Provision for bad and doubtful debts on the loan portfolio
(D) Interest accrued but not yet due on customer

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May/June 2019

5. Under which section of the Banking Regulation Act are banking companies required to prepare their financial statements in a specified format?
(A) Section 5
(B) Section 30
(C) Section 29
(D) Section 31

Ans :

(C) Section 29
Section 29 of the Banking Regulation Act mandates that banking companies must prepare their financial statements, which include the balance sheet and the profit and loss account, at the end of each accounting year. This preparation must adhere to the specific formats provided in the Third Schedule of the Act, ensuring uniformity and comparability across the industry.

Oct/Nov 2022

6. The formats for the balance sheet and profit and loss account for banking companies are prescribed in which schedule of the Banking Regulation Act?
(A) First Schedule
(B) Third Schedule
(C) Second Schedule
(D) Fourth Schedule

Ans :

(B) Third Schedule
The Banking Regulation Act specifies the structure for financial reporting to ensure consistency. The formats for the balance sheet (Form A) and the profit and loss account (Form B) that all banking companies must follow are laid down in the Third Schedule annexed to the Act. The RBI also issues guidelines to interpret these requirements.

May/June 2005

7. As per government notification, on which date must the accounts of banking companies be closed every year?
(A) 31st December
(B) 30th June
(C) 30th September
(D) 31st March

Ans :

(D) 31st March
The Government has notified that all banking companies doing business in India must close their accounts on 31st March of every year. This aligns the banking sector's financial year with the government's fiscal year. Previously, the closing date was 31st December. Banks may also close books on 30th September for internal review purposes.

Oct/Nov 2016

8. For a banking company incorporated in India, what is the minimum number of directors required to sign the financial statements, in addition to the manager or principal officer, if the board has more than three directors?
(A) Three
(B) One
(C) Two
(D) All directors

Ans :

(A) Three
Section 29 of the Banking Regulation Act specifies the signature requirements for financial statements of a bank incorporated in India. The statements must be signed by the manager or principal officer and by at least three directors. If the total number of directors is less than three, then all the directors must sign the statements.

May/June 2014

9. In the case of a foreign banking company operating in India, who is required to sign its financial statements?
(A) The Chief Executive Officer of the global parent bank from the home country
(B) At least three members of the local advisory board constituted in India
(C) The manager or agent of the principal office in India
(D) The Indian ambassador or a diplomatic official in the bank's home country

Ans :

(C) The manager or agent of the principal office in India
The signature requirements for a foreign banking company differ from those for an Indian bank. As per Section 29 of the Banking Regulation Act, the financial statements of a foreign bank's Indian operations must be signed by the manager or agent of its principal office located within India,

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May/June 2019

47. Consider the following types of deposits:
1. Fixed deposits
2. Cumulative deposits
3. Foreign Currency Non-resident Accounts
4. Matured time deposits

Which of these are included under the category 'Term Deposits' (from others)?
(A) 1 and 2 only
(B) 4 only
(C) 1, 2 and 3
(D) 1, 2, 3 and 4

Ans :

(C) 1, 2 and 3
Term deposits are repayable after a specified period. This category includes fixed deposits, cumulative and recurring deposits, and various non-resident deposits like FCNR accounts. Matured time deposits are not included here because, upon maturity, they become payable on demand and are reclassified as 'Demand Deposits' for reporting purposes.

Oct/Nov 2022

48. What is the correct treatment for interest payable on deposits that has accrued but is not yet due for payment?
(A) It is shown under Schedule 5 'Other Liabilities and Provisions'.
(B) It is ignored completely in the accounts until it becomes due for payment.
(C) It is shown as a direct deduction from 'Interest Earned' in the P&L account.
(D) It is added to the principal of the respective deposit accounts in Schedule 3.

Ans :

(A) It is shown under Schedule 5 'Other Liabilities and Provisions'.
As per the accrual concept, interest expense is recognized as it accrues over time, not just when it is paid. The amount of interest on deposits that has accrued but is not yet due for payment at the balance sheet date represents a liability for the bank. This liability is disclosed under the head 'Interest Accrued' within Schedule 5.

May/June 2005

49. Which of the following institutions' borrowings/ refinance would be classified under "Other Institutions and Agencies" in Schedule 4?
(A) Reserve Bank of India
(B) Commercial banks
(C) National Bank for Agriculture and Rural Development (NABARD)
(D) Co-operative banks

Ans :

(C) National Bank for Agriculture and Rural Development (NABARD)
Schedule 4 'Borrowings' separately classifies borrowings from the RBI and other banks. The sub-head 'Other Institutions and Agencies' is meant for borrowings and refinance obtained from specialized financial institutions like SIDBI, Export-Import Bank of India, and NABARD, as well as liability against participation certificates.

Oct/Nov 2016

50. The net balance of inter-office adjustments, if it is a credit balance, is shown under which schedule of the balance sheet?
(A) Schedule 5: Other Liabilities and Provisions
(B) Schedule 11: Other Assets
(C) Schedule 7: Balances with Banks
(D) Schedule 4: Borrowings

Ans :

(A) Schedule 5: Other Liabilities and Provisions
Inter-office adjustments represent the net amount of un-reconciled transactions between branches or between branches and the head office. A net credit balance signifies a net liability for the bank (e.g., a branch has received funds but the corresponding debit is not yet passed). This net credit balance is shown under Schedule 5.

May/June 2014

51. Which term describes money lent in the inter-bank market for a period of more than one day and up to fourteen days?
(A) Money at call
(B) Term money
(C) Notice money over a fortnight
(D) Money at short notice

Ans :

(D) Money at short notice
The inter-bank money market has specific terminology for tenors. 'Money at call' or 'call money' refers to overnight funds (lent for one day). Funds lent for a period longer than one day but up to a maximum of fourteen days are specifically referred to as 'money at short notice'. Both are reported under Schedule 7.

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(C) Other Expenditure
(D) Insurance

Ans :

(D) Insurance
Schedule 16 'Operating Expenses' has a specific head for 'Insurance'. This category is comprehensive and includes all insurance charges incurred by the bank to mitigate various risks. It covers premiums for insuring bank property, cash, as well as specific operational risk policies like those for DICGC, Employee Fidelity, Fraud Covers, and emerging threats like Cyber Risks.

Oct/Nov 2012

72. Which of the following is a 'contra item' that appears on both the asset and liability sides of a bank's balance sheet presentation?
(A) Term Loans, representing a claim on borrowers
(B) Acceptances, Endorsements and Other Obligations
(C) Statutory Reserve, representing retained earnings
(D) Rebate on Bills Discounted, representing unearned income

Ans :

(B) Acceptances, Endorsements and Other Obligations
A contra item reflects a situation where the bank has an obligation to a third party, but also a corresponding claim on its customer. For acceptances and endorsements, the bank's obligation is shown as a liability, while the customer's counter-guarantee to the bank is shown as an asset (Constituents' Liability). These items offset each other.

May/June 2011

73. A bank's investment in gold is shown under the head 'Investment', but its investment in silver is shown under which head?
(A) Investment
(B) Cash and Balances with RBI
(C) Other assets
(D) Fixed Assets

Ans :

(C) Other assets
While both are precious metals, gold and silver receive different accounting treatments in a bank's balance sheet. Gold is considered a financial asset and is classified under 'Investment' in Schedule 8. Silver, however, is not given the same status and any holdings of it are to be shown under the residual category of 'other assets' in Schedule 11.

Oct/Nov 2020

74. Every banking company incorporated in India is required to transfer a sum equal to what percentage of its net profit to a reserve fund before declaring any dividend?
(A) 20%
(B) 10%
(C) 15%
(D) 25%

Ans :

(A) 20%
To strengthen the financial position and build up reserves, the law mandates a compulsory transfer of profits. Every Indian banking company must, before declaring a dividend, transfer a minimum of twenty per cent (20%) of the net profit for the year to its statutory reserve fund. This ensures a portion of earnings is retained within the bank.

May/June 2022

75. To maintain uniformity, the RBI Master Circular of July 1, 2015, specifies that the 'Summary of Significant Accounting Policies' and 'Notes to Accounts' are to be shown under which schedules, respectively?
(A) Schedule 15 and Schedule 16
(B) Schedule 17 and Schedule 18
(C) Schedule 16 and Schedule 17
(D) Schedule 18 and Schedule 19

Ans :

(B) Schedule 17 and Schedule 18
To enhance clarity and comparability of financial statements, the RBI has standardized the location of key disclosures. The 'Summary of Significant Accounting Policies' is to be presented under Schedule 17, and all other detailed 'Notes to Accounts' are to be furnished under Schedule 18, following the main financial statements and their supporting schedules 1 to 16.

Oct/Nov 2023

76. **Assertion (A) :** A bank cannot afford to ignore updating its customer ledgers and must enter every transaction as soon as it takes place.
Reason (R) : Banks follow the mercantile system

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granted to the Central and State Governments, as well as to Government Companies and Corporations, are specifically categorized under the 'Public sector' head. This is distinct from 'Priority Sectors', which is defined by RBI instructions for specific economic activities.

May/June 2010

57. What is the correct accounting treatment for credit card outstanding balances?
(A) They should be shown under 'Other Assets' in Schedule 11
(B) They should be shown under 'Inter-office adjustments' in Schedule 11
(C) They should be shown under 'Contingent Liabilities' in Schedule 12
(D) They should be shown as part of 'Advances' in Schedule 9

Ans :

(D) They should be shown as part of 'Advances' in Schedule 9
A credit card outstanding balance represents an amount lent by the bank to the cardholder. It is a form of unsecured personal loan. Therefore, the general notes on disclosures explicitly state that credit card outstanding amounts are not to be included under 'Other Assets' but must be correctly classified and shown as part of 'Advances'.

Oct/Nov 2024

58. Non-interest bearing loans and advances given to staff by a bank acting as an employer are shown under which head?
(A) 'Others' under 'Other Assets' in Schedule 11
(B) 'Advances' in Schedule 9
(C) 'Payments to and Provisions for Employees' in Schedule 16
(D) 'Fixed Assets' in Schedule 10

Ans :

(A) 'Others' under 'Other Assets' in Schedule 11
The classification depends on whether the bank is acting as a banker or an employer. When a non-interest-bearing advance is given to a staff member (e.g., for a festival or emergency), the bank is acting as an employer. Such advances are not treated as regular loans and are instead reflected under the 'Others' sub-head within Schedule 11 'Other Assets'.

May/June 2017

59. When a bank accepts a bill of exchange on behalf of a customer, this obligation is recorded under which head in the Balance Sheet?
(A) Schedule 4: Borrowings, as it is a form of short-term funding
(B) Schedule 5: Other Liabilities and Provisions, as it is a payable
(C) Schedule 12: Contingent Liabilities as 'Acceptances, Endorsements and Other Obligations'
(D) Schedule 9: Advances, as it represents credit extended to the customer

Ans :

(C) Schedule 12: Contingent Liabilities as 'Acceptances, Endorsements and Other Obligations'
When a bank accepts a bill on behalf of a customer, it creates a contingent liability. The bank takes upon itself the responsibility for payment if the customer fails to do so. This obligation, along with endorsements and letters of credit, is disclosed off-balance sheet under the specific head 'Acceptances, Endorsements and Other Obligations' in Schedule 12.

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Oct/Nov 2005

60. According to the general instructions for compilation of financial statements, figures should be rounded off to the nearest:
(A) Rupee
(B) Thousand rupees
(C) Hundred rupees
(D) Lakh rupees

Ans :

(B) Thousand rupees
To ensure clarity and conciseness in financial statements involving large figures, the general instructions for compilation specify a standard for rounding off. All figures presented in the balance sheet and profit and loss account should be rounded off to the nearest thousand rupees. For example, a sum of ₹19,75,921.20 would appear as ₹19,76.

May/June 2020

61. The amount of provision for taxation is charged to the Profit and Loss Account under which heading?
(A) Interest Expended
(B) Operating Expenses

(C) Provisions and Contingencies
(D) Other Income

Ans :

(C) Provisions and Contingencies
The Profit and Loss Account format includes a specific line item for all major provisions. The estimated amount of income tax liability for the year is charged to the P&L under the heading 'Provisions and Contingencies'. This heading also includes provisions for bad debts and diminution in the value of investments, grouping all such non-cash charges together.

Oct/Nov 2015

62. What does 'Rebate on Bills Discounted' represent?
(A) A preferential, non-standard discount rate offered exclusively to a bank's most valued prime customers
(B) A cash refund of a portion of the discount, given back to the customer as a reward for making an early payment on a bill
(C) A separate fee or commission, distinct from the discount rate, that is charged by the bank for the service of discounting a bill
(D) Unearned discount income related to the portion of a bill's tenor that falls into the next financial year

Ans :

(D) Unearned discount income related to the portion of a bill's tenor that falls into the next financial year
'Rebate on Bills Discounted' is also known as unearned discount. When a bank discounts a bill, it receives income for the entire tenor of the bill upfront. If the bill's maturity extends beyond the current financial year, the portion of the discount income related to the subsequent year is considered unearned and is carried forward as a liability.

May/June 2013

63. What is the accounting entry to record the unearned discount at the end of the financial year?
(A) Rebate on Bills Discounted a/c Dr. To Discount a/c
(B) Profit & Loss a/c Dr. To Rebate on Bills Discounted a/c
(C) Discount a/c Dr. To Rebate on Bills Discounted a/c
(D) Bills Discounted a/c Dr. To Rebate on Bills Discounted a/c

Ans :

(C) Discount a/c Dr. To Rebate on Bills Discounted a/c
To correctly match income with the period it is earned, the unearned portion of the discount must be removed from the current year's income. This is achieved by debiting the Discount account (reducing the income) and crediting the 'Rebate on Bills Discounted' account, which is a liability account shown in the balance sheet.

Oct/Nov 2021

64. In the format of the Profit and Loss Account (Form B), 'Interest Earned' is detailed in which schedule?
(A) Schedule 12
(B) Schedule 14
(C) Schedule 15
(D) Schedule 13

Ans :

(D) Schedule 13
Form B, the format for the Profit and Loss Account, is supported by schedules that provide detailed breakdowns of income and expenditure. Schedule 13, titled 'Interest Earned', is the first schedule and it lists all the major sources of interest income for the bank, such as interest on advances, income on investments, and interest on inter-bank funds.

May/June 2024

65. Which of the following items would be classified under Schedule 14 'Other Incomes'?
(A) Commission, exchange and brokerage
(B) Interest on term loans
(C) Interest on government securities
(D) Interest on savings bank deposits

Ans :

(A) Commission, exchange and brokerage
Schedule 14 'Other Incomes' captures all revenue that is not in the nature of interest. This includes fee-based income such as commission on remittances and letters of credit, exchange brokerage, profit on sale of assets, and dividends from subsidiaries. Interest income from loans and investments is reported under Schedule 13 'Interest Earned'.

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Oct/Nov 2008

66. 'Payments to and Provisions for Employees' is a major head of expenditure shown under which schedule of the P&L Account?
(A) Schedule 13
(B) Schedule 16
(C) Schedule 14
(D) Schedule 15

Ans :

(B) Schedule 16
Schedule 16, 'Operating Expenses', details the various non-financial costs incurred by the bank in its day-to-day operations. The very first item under this schedule is 'Payments to and Provisions for Employees', which includes salaries, allowances, bonuses, provident fund contributions, and other staff-related expenses, making it a significant component of the bank's cost structure.

May/June 2006

67. The profit or loss on the revaluation of investments is included under which schedule of the Profit and Loss account?
(A) Schedule 13: Interest Earned
(B) Schedule 15: Interest Expended
(C) Schedule 16: Operating Expenses
(D) Schedule 14: Other Incomes

Ans :

(D) Schedule 14: Other Incomes
Gains or losses arising from marking investments to market (revaluation) are a form of non-interest income or expense. As per the prescribed format, the net profit or loss on the revaluation of investments is shown under Schedule 14 'Other Incomes'. This is distinct from the net profit or loss on the actual sale of investments, which is also shown here.

Oct/Nov 2017

68. Which of the following is an example of an item included in Schedule 15 'Interest Expended'?
(A) Interest on RBI/Inter-Bank Borrowings
(B) Interest on cash credit accounts
(C) Staff salaries and allowances
(D) Commission paid to agents

Ans :

(A) Interest on RBI/Inter-Bank Borrowings
Schedule 15 'Interest Expended' details the interest costs incurred by the bank. This primarily includes interest paid on various types of deposits from customers. It also includes interest paid on borrowings from the Reserve Bank of India and other banks in the inter-bank market, which is a key component of the bank's cost of funds.

May/June 2008

69. House rent allowance paid to staff should be included under which head in the P&L schedules?
(A) Rent, Taxes and Lighting
(B) Other Expenditure
(C) Payments to and Provisions for Employees
(D) Miscellaneous Income

Ans :

(C) Payments to and Provisions for Employees
The classification of expenses should be based on their nature. House rent allowance is a part of the compensation package for employees. Therefore, it should not be clubbed with rent paid for premises under 'Rent, Taxes and Lighting'. It must be correctly included under Schedule 16 in the head 'Payments to and Provisions for Employees'.

Oct/Nov 2013

70. According to the notes on Schedule 14, if any item under 'Miscellaneous Income' exceeds what percentage of the total income, should particulars be given in the notes?
(A) 1%
(B) 2%
(C) 5%
(D) 10%

Ans :

(A) 1%
To ensure material items are not hidden within a broad miscellaneous category, a disclosure threshold is set. The instructions for Schedule 14 'Other Incomes' state that if any single item included under the sub-head 'Miscellaneous Income' is significant, its particulars should be disclosed separately in the notes. The threshold for significance is defined as exceeding one percent of the total income.

May/June 2015

71. Insurance premium paid to DICGC and for coverage of cyber risks are included under which head of Operating Expenses in Schedule 16?
(A) Law Charges
(B) Repairs and Maintenance

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(C) 15%
(D) 40%

Ans :

(D) 40%
Provisioning for the secured portion of a doubtful asset increases with time. For an asset that has been doubtful for up to one year, the provision is 25%. For assets that have been doubtful for a period of one to three years, the required provision on the secured portion increases to 40%.

Oct/Nov 2014

82. Match List-I (Asset Category) with List-II (Provisioning Requirement).
List-I
P. Standard Asset (Direct Agriculture)
Q. Sub-Standard Asset
R. Loss Asset
S. Doubtful Asset (unsecured portion)
List-II
1. 15% on total outstanding
2. 100% of total outstanding
3. 0.25% of outstanding
4. 100% of the unsecured exposure
(A) P-3, Q-1, R-2, S-4
(B) P-1, Q-3, R-4, S-2
(C) P-3, Q-2, R-1, S-4
(D) P-2, Q-4, R-3, S-1

Ans :

(A) P-3, Q-1, R-2, S-4
The provisioning norms are specific to each asset category. A standard agricultural asset requires a 0.25% provision. A sub-standard asset requires a general provision of 15%. A loss asset, where the loss has been identified, requires a 100% provision. The unsecured portion of a doubtful asset also requires a 100% provision.

May/June 2021

83. Bank investments are classified by RBI into three categories. Which of the following is NOT one of those categories?
(A) Held to maturity (HTM)
(B) Available for sale (AFS)
(C) Designated at fair value (DAFV)
(D) Held for trading (HFT)

Ans :

(C) Designated at fair value (DAFV)
As per RBI guidelines, banks are required to classify their investment portfolio into three distinct categories for valuation and accounting purposes. These categories are 'Held to maturity' (HTM), 'Available for sale' (AFS), and 'Held for trading' (HFT). 'Designated at fair value' is a term used in other accounting standards but not one of the three primary RBI categories.

Oct/Nov 2006

84. The 'Held to Maturity' (HTM) category of investments should not exceed what percentage of the bank's total investments?
(A) 10%
(B) 50%
(C) 75%
(D) 25%

Ans :

(D) 25%
The 'Held to Maturity' category is intended for securities that the bank intends and is able to hold until maturity. To limit the portion of the portfolio that is not marked to market, the RBI has stipulated that the investments included under the HTM category should not exceed 25% of the bank's total investments.

May/June 2016

85. What is the mandated time frame within which securities classified as 'Held for Trading' (HFT) are to be sold?
(A) 90 days
(B) 30 days
(C) 180 days
(D) 365 days

Ans :

(A) 90 days
The 'Held for Trading' (HFT) category is for securities acquired with the intention of trading to take advantage of short-term price or interest rate movements. Reflecting this short-term intent, the guidelines mandate that securities classified under the HFT category are to be sold within a period of ninety days from the date of acquisition.

Oct/Nov 2025

86. Which categories of a bank's investment portfolio must be marked to market?
(A) Only Held to Maturity (HTM)
(B) Both Available for Sale (AFS) and Held for Trading (HFT)
(C) Only Available for Sale (AFS)

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of accounting, which requires immediate posting to all ledgers.

(A) Both (A) and (R) are true and (R) is the correct explanation of (A)
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A)
(C) (A) is true but (R) is false
(D) (A) is false but (R) is true

Ans :

(C) (A) is true but (R) is false
Assertion (A) is true; the need for accuracy and up-to-date customer accounts is paramount in banking. However, Reason (R) is false. While banks do follow the mercantile system, this system itself does not mandate immediate posting. The operational need for real-time customer account information is the primary driver for this practice, not a feature of mercantile accounting itself.

May/June 2018

77. A term loan account is classified as a Non-Performing Asset (NPA) if the interest and/or instalment of principal remains overdue for a period of more than:

(A) 30 days
(B) 60 days
(C) 180 days
(D) 90 days

Ans :

(D) 90 days
The Reserve Bank of India has stipulated clear norms for asset classification. An advance is classified as a non-performing asset based on the period it remains overdue. For a term loan, if either the interest payment or the principal instalment is not received and remains overdue for more than 90 days, the account is categorized as an NPA.

Oct/Nov 2018

78. What is the income recognition policy for Non-Performing Assets (NPAs)?

(A) Income is recognised on a cash basis
(B) Income is recognised on an accrual basis
(C) 50% of the income is recognised on an accrual basis and 50% on a cash basis
(D) No income can be recognised until the asset becomes a performing asset again

Ans :

(A) Income is recognised on a cash basis
To ensure that banks' profits are not overstated with unrealized income, a conservative approach is mandated for NPAs. Unlike performing assets where income is recognized on an accrual basis, any income (like interest) from an NPA can only be recognized in the profit and loss account when it is actually received in cash by the bank.

May/June 2007

79. An asset that has remained in the sub-standard category for a period of 12 months is classified as a:

(A) Standard Asset
(B) Sub-standard Asset
(C) Doubtful Asset
(D) Loss Asset

Ans :

(C) Doubtful Asset
Asset classification follows a progressive deterioration path. An asset first becomes sub-standard. If it continues to exhibit credit weakness and remains in the sub-standard category for a period of 12 months, it is then downgraded to the 'Doubtful Asset' category, which requires a higher level of provisioning based on the age of the asset and security available.

Oct/Nov 2009

80. What is the provisioning requirement for the unsecured portion of a doubtful asset?

(A) 100%
(B) 25%
(C) 40%
(D) 75%

Ans :

(A) 100%
The provisioning norms for doubtful assets are stringent, especially for the unsecured part. The unsecured portion of any doubtful asset, which is the part not covered by the realizable value of security, is considered highly risky. Therefore, prudential norms require a full 100% provision to be made against this unsecured exposure, regardless of how long it has been doubtful.

May/June 2012

81. For a secured doubtful asset that has been in the doubtful category for two years, what is the required provision?

(A) 25%
(B) 100%

Oct/Nov 2007

52. What is the prescribed accounting treatment for the difference between the book value and market value of government securities held by a bank?

(A) It is ignored in all disclosures as these are considered risk-free sovereign securities
(B) The difference should be given in the notes to the balance sheet
(C) It should be adjusted against the Capital account directly without affecting profits
(D) It is shown under the 'Provisions and Contingencies' line item in the Profit and Loss account

Ans :

(B) The difference should be given in the notes to the balance sheet
While government securities are shown at book value in Schedule 8 'Investments', transparency requires the disclosure of their current market worth. The instructions specify that the difference between the book value and the market value of these securities should be disclosed in the 'Notes to Accounts', providing stakeholders with information about potential unrealized gains or losses.

May/June 2025

53. Which of the following is NOT classified under 'Other approved securities' in Schedule 8?

(A) Securities other than Government Securities treated as approved under the BR Act, 1949
(B) Bonds of public sector undertakings that are approved for SLR purposes
(C) Central and State Government securities
(D) Debentures of corporations specified as approved securities by the regulator

Ans :

(C) Central and State Government securities
Schedule 8 has a distinct category for 'Government securities', which includes Central and State Government securities and Treasury Bills. 'Other approved securities' is a separate category for securities that, while not issued by the government, are treated as approved securities for statutory purposes as per the provisions of the Banking Regulation Act, 1949.

Oct/Nov 2019

54. How is a loan classified where the borrower repays in installments over a period exceeding one year?

(A) Demand Loan
(B) Overdraft
(C) Cash Credit
(D) Term Loan

Ans :

(D) Term Loan
A term loan is a type of advance given for a fixed term, typically exceeding one year, with a pre-determined repayment schedule, often in installments. This contrasts with a demand loan, which is repayable on demand and usually for a short period not exceeding a year. Overdrafts and cash credits are running facilities.

May/June 2009

55. Advances covered by the guarantee of the Deposit Insurance and Credit Guarantee Corporation (DICGC) are classified under which category of security in Schedule 9?

(A) Covered by bank/Govt. guarantees
(B) Secured by tangible assets
(C) Unsecured
(D) Priority Sector

Ans :

(A) Covered by bank/Govt. guarantees
Schedule 9 classifies advances based on the nature of the security. Advances that are not secured by tangible assets but are backed by guarantees from governments (Indian or foreign), other banks, or specific government bodies like DICGC, ECGC, and CGTS are classified under the head 'Covered by bank/Govt. guarantees'.

Oct/Nov 2011

56. Advances to Central and State Governments and other government undertakings are classified under which sectoral category in Section 'C' of Schedule 9?

(A) Priority Sectors
(B) Public sector
(C) Banks
(D) Others

Ans :

(B) Public sector
Section 'C' of Schedule 9 requires a sectoral classification of advances in India. Advances

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(D) Only Held for Trading (HFT)

Ans :

(B) Both Available for Sale (AFS) and Held for Trading (HFT)
The valuation rules differ by investment category. Securities in the 'Held to Maturity' (HTM) category are carried at acquisition cost and not marked to market. However, securities classified under both 'Available for Sale' (AFS) and 'Held for Trading' (HFT) categories, which are considered the current/trading portion of the portfolio, must be revalued to their market price periodically.

May/June 2023

87. What is the primary purpose of Pillar 3 disclosures under the Basel-III framework?
(A) To set the absolute minimum capital requirements for all banks
(B) To outline the detailed supervisory review process for regulators
(C) To encourage market discipline through a set of disclosure requirements
(D) To prescribe the mandatory internal models for credit risk measurement

Ans :

(C) To encourage market discipline through a set of disclosure requirements
The Basel framework is built on three pillars. Pillar 3, known as Market Discipline, aims to complement Pillar 1 (Minimum Capital Requirements) and Pillar 2 (Supervisory Review). It does this by requiring banks to make a set of disclosures that allow market participants to assess key information on the bank's capital, risk exposures, and risk management processes.

Oct/Nov 2010

88. Pillar 3 disclosures as introduced under Basel III became effective from which date?
(A) July 1, 2013
(B) April 1, 2018
(C) March 31, 2015
(D) January 1, 2019

Ans :

(A) July 1, 2013
The implementation of the Basel III framework was a phased process. The disclosure requirements under Pillar 3, which are designed to enhance market discipline and transparency in the banking sector, were made effective in India from July 1, 2013, as per the directives issued by the Reserve Bank of India.

May/June 2019

89. According to Basel III guidelines, how frequently are banks required to make Pillar 3 disclosures on Capital Adequacy and Credit Risk?
(A) On a monthly basis
(B) On a half-yearly basis
(C) On a quarterly basis
(D) On an annual basis

Ans :

(C) On a quarterly basis
While most Pillar 3 disclosures are required at least half-yearly, certain critical disclosures need more frequent updates. The guidelines specify that disclosures related to (i) Capital Adequacy, (ii) Credit Risk: General Disclosures, and (iii) Credit Risk: Disclosures for Portfolios Subject to the Standardised Approach must be made by banks at least on a quarterly basis.

Oct/Nov 2022

90. Banks listed on a stock exchange in India must comply with the requirements of which regulation?
(A) SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015
(B) Banking Regulation Act, 1949
(C) Companies Act, 2013
(D) RBI Master Circular on Basel III

Ans :

(A) SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015
While all banks are governed by the BR Act and RBI circulars, banks whose shares are listed on a stock exchange have an additional layer of regulation. They must comply with the rules set by the market regulator, SEBI. The primary regulation governing their conduct is the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, as amended.

May/June 2005

91. The implementation of Indian Accounting Standards (Ind AS) for Scheduled Commercial Banks (excluding RRBs) was initially planned for April 1, 2018, but was subsequently deferred. What was one of the key reasons for this deferment?
(A) A shortage of qualified accountants with

NODIA

sufficient practical training in the complex new Ind AS standards
(B) Strong resistance from foreign banks in India, who cited the complexities of dual reporting burdens
(C) A global strategic decision by the IASB to postpone the IFRS 9 implementation timeline for all financial institutions
(D) The need for legislative amendments to the Banking Regulation Act's prescribed financial statement formats

Ans :

(D) The need for legislative amendments to the Banking Regulation Act's prescribed financial statement formats
The transition to Ind AS required significant changes. A primary reason for the deferment was that the format of financial statements prescribed in the Third Schedule of the Banking Regulation Act, 1949, was not compatible with the presentation requirements under Ind AS. Necessary legislative amendments were under consideration by the Government, prompting the RBI to defer implementation.

Oct/Nov 2016

92. As per RBI's advisory, what is the role of the Audit Committee of the Board in the Ind AS implementation process?
(A) To lead the bank's internal Steering Committee for day-to-day implementation
(B) To oversee the progress of the implementation process and report to the Board quarterly
(C) To directly manage the project, allocate necessary resources, and hire consultants
(D) To conduct the final statutory audit of the first Ind AS compliant financial statements

Ans :

(B) To oversee the progress of the implementation process and report to the Board quarterly
The RBI has defined a clear governance structure for the Ind AS transition. While a Steering Committee manages the day-to-day process, the Audit Committee of the Board is entrusted with the critical oversight function. It is responsible for monitoring the progress of the implementation and reporting on it to the full Board of Directors at quarterly intervals.

May/June 2014

93. Which of the following is NOT considered a 'Subsidiary book' in the context of books of account maintained by banks?
(A) Current account ledger
(B) Loan ledger
(C) General ledger
(D) Bills discounted and purchased ledger

Ans :

(C) General ledger
Subsidiary books or ledgers contain the detailed, individual accounts that support a control account. The Current account ledger, Loan ledger, and Bills discounted ledger are all examples of subsidiary books. The General Ledger, however, is the principal book of account that contains all the control accounts, asset, liability, income, and expense accounts, not a subsidiary book.

Oct/Nov 2007

94. Rebate on bills discounted is conceptually related to which of the following accounting principles?
(A) Business Entity Concept
(B) Money Measurement Concept
(C) Dual Aspect Concept
(D) Matching Principle

Ans :

(D) Matching Principle
Rebate on bills discounted, or unearned income, is an adjustment made to comply with the matching principle. This principle dictates that revenues should be recognized in the period in which they are earned. By separating the unearned portion of the discount, banks ensure that only the income pertaining to the current accounting period is credited to the P&L account.

May/June 2025

95. Which of the following statements about the preparation of a bank's financial statements is INCORRECT?
(A) A banking company must transfer 25% of its current year's profit to the Statutory Reserve
(B) A Profit and Loss Appropriation account is not separately prepared
(C) Appropriations like transfer to statutory reserve are shown in the balance sheet
(D) The words 'To' and 'By' are not used in the profit and loss account

Ans :

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(A) A banking company must transfer 25% of its current year's profit to the Statutory Reserve
Banks follow specific conventions in preparing final accounts. A separate P&L Appropriation account is not made; appropriations are shown in the balance sheet. The P&L format omits 'To' and 'By'. However, the mandatory transfer to Statutory Reserve before declaring a dividend is twenty percent (20%) of the net profit, not twenty-five percent.

Oct/Nov 2019

96. Based on the rule provided, if a bank's financial year ends on March 31, 2023, what is the latest date by which its audited accounts must be published in a newspaper?
(A) June 30, 2023
(B) September 30, 2023
(C) July 31, 2023
(D) December 31, 2023

Ans :

(B) September 30, 2023
The rule states that publication must happen within six months from the end of the related period. For a financial year ending on March 31, 2023, the six-month period concludes on September 30, 2023. Therefore, the bank must publish its accounts and auditor's report in the specified newspaper by this deadline to comply with the regulation.

May/June 2009

97. A bank lends ₹50 crores to another bank for a period of 10 days in the inter-bank market. Based on the source text, how would this transaction be classified?
(A) Money at call
(B) Term money
(C) Inter-bank deposit
(D) Money at short notice

Ans :

(D) Money at short notice
The provided text clearly defines the terminology for inter-bank lending tenors. Since the funds are lent for 10 days, which is a period more than one day and not exceeding fourteen days, the transaction correctly falls under the classification of 'money at short notice'. 'Money at call' is strictly for overnight, or one-day, lending.

Oct/Nov 2011

98. A customer has a sanctioned cash credit limit of ₹10 lakhs. Over a month, the customer withdraws ₹4 lakhs and later repays ₹1 lakh. The interest for the period will be calculated on what basis, according to the source?
(A) On the amount actually drawn from time to time
(B) On the sanctioned limit of ₹10 lakhs
(C) On the net amount of ₹3 lakhs
(D) On the maximum withdrawal of ₹4 lakhs

Ans :

(A) On the amount actually drawn from time to time
The source highlights a key advantage of cash credit. It explicitly states that interest is payable only on the amount actually drawn at any given time, not on the entire sanctioned limit. The ability to draw funds as needed and repay surpluses means the interest burden is linked directly to the funds utilized by the borrower.

May/June 2010

99. A bank revalues its head office building, resulting in a surplus of ₹5 crores. According to the provided text, how should the bank treat this surplus?
(A) Credit it to the Profit and Loss account as 'Other Income'
(B) Distribute it to shareholders as a special dividend
(C) Treat it as a capital reserve, which is not available for profit distribution
(D) Use it to write off bad debts for the year

Ans :

(C) Treat it as a capital reserve, which is not available for profit distribution
The source clearly stipulates the treatment for such gains. A surplus on the revaluation of assets is an unrealized gain and is not considered free for distribution. It must be classified as a capital reserve, meaning it increases the bank's net worth but cannot be paid out as dividends or treated as distributable profit.

Oct/Nov 2024

100. An advance of ₹10 lakh becomes an NPA on April 1, 2021. On May 1, 2022, the realizable value of security is ₹6 lakh. Based on the table, what is the total provision required as of May 1, 2022?
(A) ₹1,50,000

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Ans :

(C) ₹2,00,000
The total advances are classified by security. Unsecured advances are the portion of total advances that are not secured by tangible assets or covered by guarantees.
Total Advances = ₹38,00,000.
Secured portion = ₹30,00,000 (Tangible) + ₹6,00,000 (Guarantees) = ₹36,00,000.
Unsecured Advances = Total Advances - Secured portion = ₹38,00,000 - ₹36,00,000 = ₹2,00,000.

Oct/Nov 2017

110. For Vikas Bank, what is the amount to be shown against 'Payment to and Provision for Employees' in Schedule 16, after making necessary adjustments?
(A) ₹4,37,467
(B) ₹4,45,467
(C) ₹5,73,192
(D) ₹3,97,467

Ans :

(A) ₹4,37,467
The head 'Payment to and Provision for Employees' should include salaries and allowances but exclude Director's fees, which are shown separately. The chief executive's remuneration is an employee cost.
Total given under Salaries etc. = ₹4,45,467.
Less: Director's fees included = ₹8,000.
Amount for 'Payment to... Employees' = ₹4,45,467 - ₹8,000 = ₹4,37,467.

May/June 2008

111. Calculate the 'Provision for Income Tax' for Vikas Bank Ltd. for the year.
(A) ₹6,91,793
(B) ₹2,07,538
(C) ₹35,000
(D) ₹2,42,128

Ans :

(D) ₹2,42,128
The provision for income tax is calculated by applying the given tax rate to the profit before tax.
Profit before Tax = ₹6,91,793.
Tax Rate = 35%.
Provision for Income Tax = ₹6,91,793 × 35% = ₹2,42,127.55.
Rounding to the nearest rupee as shown in the solution, the amount is ₹2,42,128.

Oct/Nov 2013

112. What is the amount that Vikas Bank Ltd. must transfer to the Statutory Reserve for the year?
(A) ₹4,49,665
(B) ₹89,933
(C) ₹1,12,416
(D) ₹2,24,833

Ans :

(B) ₹89,933
Banks are required to transfer 20% of their net profit for the year to the Statutory Reserve before declaring dividends.
Net Profit after Tax = ₹4,49,665.
Transfer to Statutory Reserve = 20% of ₹4,49,665 = ₹89,933.
This appropriation is a mandatory step to strengthen the bank's reserve position as per regulatory requirements.

May/June 2015

113. What is the total gross value of 'Advances' that should be reported in Schedule 9 for Vikas Bank Ltd.?
(A) ₹48,00,000
(B) ₹32,08,000
(C) ₹48,08,000
(D) ₹47,92,000

Ans :

(C) ₹48,08,000
Schedule 9 reports the gross value of all advances before provisions. The total is the sum of all loan types.
Total Advances = Term Loans (₹10,00,000) + CC Hypothecation (₹12,64,000) + CC Pledge (₹9,44,000) + Bills Purchased (₹16,00,000) = ₹48,08,000. The provision for the doubtful advance is accounted for under 'Provisions and Contingencies', not as a deduction from the gross advance figure here.

Oct/Nov 2012

114. Based on the available data, what is the total of 'Others (including provisions)' under Schedule 5 for Vikas Bank Ltd.?
(A) ₹2,90,128
(B) ₹56,000
(C) ₹2,50,128
(D) ₹2,98,128

Ans :

(D) ₹2,98,128

NODIA

This means the figure reported should represent the total amount receivable from the borrower, comprising both the regular outstanding principal and any instalments that have become due but have not yet been paid.

May/June 2013

105. A bank's Head Office account shows a debit of ₹10 Cr, and its Branch account shows a credit of ₹8 Cr. As per the source, what will be shown in the final accounts?

(A) A debit of ₹10 Cr and a credit of ₹8 Cr shown separately in the notes
(B) A net credit balance of ₹2 Cr under 'Other Liabilities'
(C) A net debit balance of ₹2 Cr under 'Other Assets'
(D) An aggregate balance of ₹18 Cr under 'Contingent Liabilities'

Ans :

(C) A net debit balance of ₹2 Cr under 'Other Assets'
The source mandates that only the net balance of all inter-office accounts should be shown. By aggregating a debit of ₹10 Cr and a credit of ₹8 Cr, the resulting net balance is a debit of ₹2 Cr. A net debit balance in inter-office adjustments is classified as an asset and would be shown under Schedule 11 'Other Assets'.

Oct/Nov 2021

106. Based on the case data, what is the total 'Interest Earned' to be shown in Schedule 13 of ABC Bank's Profit and Loss Account?

(A) ₹7,45,000
(B) ₹6,90,000
(C) ₹6,35,000
(D) ₹7,00,000

Ans :

(B) ₹6,90,000
Interest Earned (Schedule 13) is calculated by summing up all interest and discount income and then adjusting for unexpired discount.
Total Interest = ₹2,80,000 (Loan) + ₹2,40,000 (CC) + ₹60,000 (Overdraft) = ₹5,80,000.
Discount earned = ₹1,65,000 - ₹55,000 (Unexpired) = ₹1,10,000.
Total Interest Earned = ₹5,80,000 + ₹1,10,000 = ₹6,90,000.

May/June 2024

107. What is the total 'Operating Expenses' to be reported in Schedule 16 for ABC Bank Ltd.?

(A) ₹92,000
(B) ₹65,000
(C) ₹87,000
(D) ₹94,000

Ans :

(D) ₹94,000
Schedule 16 'Operating Expenses' includes all non-interest expenses. To find the total, we sum up all the given expense items:
Establishment Expenses (₹60,000) + Audit Fees (₹5,000) + Rent and Taxes (₹22,000) + Postage and Telegrams (₹2,000) + Printing and Stationery (₹3,000) + Sundry Expenses (₹2,000) equals a total of ₹94,000.

Oct/Nov 2008

108. For Modern Bank Ltd., the total income is ₹3,34,000. The interest expended is ₹2,20,190 and operating expenses are ₹75,000. The solution in the book shows a total expenditure of ₹2,95,190, implying no other provisions. What is the Net Profit for the year?

(A) ₹38,810
(B) ₹63,810
(C) ₹1,13,810
(D) ₹2,59,000

Ans :

(A) ₹38,810
Net Profit is calculated as Total Income minus Total Expenditure.
Total Income = ₹3,34,000.
Total Expenditure = Interest Expended (₹2,20,190) + Operating Expenses (₹75,000) = ₹2,95,190.
Net Profit = ₹3,34,000 - ₹2,95,190 = ₹38,810. This matches the profit figure shown in the solved illustration, confirming the expenditure components.

May/June 2006

109. Based on the provided data for Punjab Bank Ltd., what is the value of 'Unsecured' advances to be shown in Schedule 9?

(A) ₹4,00,000
(B) ₹8,00,000
(C) ₹2,00,000
(D) ₹32,00,000

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May/June 2023

129. If the net position of 'Profit on Sale of Investments' and 'Loss on Sale of Investments' is a loss, how is it shown in Schedule 14?

(A) The net loss is ignored and only the gross profit is shown

(B) It is shown as a positive figure under a separate head 'Net Loss on Investments'

(C) The loss figure is shown in brackets as a deduction

(D) The net loss is transferred directly to the Investment Fluctuation Reserve

Ans :

(C) The loss figure is shown in brackets as a deduction

Schedule 14 requires the net position to be reported. The format is 'Profit on Sale of Investments' Less 'Loss on Sale of Investments'. If the result is a net loss, the note to the schedule specifies that the loss figure should be shown in brackets, indicating a negative amount or a deduction from other incomes.

Oct/Nov 2010

130. A bank maintains a register for 'Bills for collection'. On collection of a bill, the bank passes an accounting entry. Which of the following correctly represents this entry?

(A) Cash Account Dr.; To Customer's Account; To Commission Account

(B) Customer's Account Dr.; To Cash Account; To Commission Account

(C) Bills for Collection Account Dr.; To Customer's Account

(D) Cash Account Dr.; To Bills for Collection Account

Ans :

(A) Cash Account Dr.; To Customer's Account; To Commission Account

Upon successful collection, the bank receives cash, so the Cash Account is debited. The net proceeds (amount collected less commission) belong to the customer, so the Customer's Account is credited. The bank's income, the commission, is credited to the Commission Account. This entry correctly reflects the settlement of the collection transaction and recognizes the bank's revenue.

NODIA

The 'Others' sub-head in Schedule 5 includes various provisions and unearned income. Based on the case data and calculations:
Unexpired Discount (Rebate) = ₹48,000.
Provision for Taxation = ₹2,42,128.
Provision for Bad Debts = ₹8,000.
Total = ₹48,000 + ₹2,42,128 + ₹8,000 = ₹2,98,128.
This represents the total amount under this category.

May/June 2011

115. What is the net amount of 'Interest/Discount on Advances/Bills' to be shown in Schedule 13 for Vikas Bank Ltd.?
(A) ₹17,33,400
(B) ₹18,29,400
(C) ₹17,81,400
(D) ₹12,38,400

Ans :

(A) ₹17,33,400
Schedule 13 'Interest Earned' combines interest received and net discount earned.
Interest Received = ₹12,86,400.
Net Discount Earned = Total Discount (₹4,95,000) - Unexpired Discount (₹48,000) = ₹4,47,000.
Total Interest/Discount = ₹12,86,400 + ₹4,47,000 = ₹17,33,400. This is the total income from interest and discount activities for the year.

Oct/Nov 2020

116. Consider the following statements regarding accounting systems in banks:
1. Banks follow the 'voucher posting' system.
2. Relatively greater emphasis is placed on books of prime entry like journals.

Which of the statements is/are correct?
(A) 1 only
(B) 2 only
(C) Both 1 and 2
(D) Neither 1 nor 2

Ans :

(A) 1 only
Banks typically follow the 'voucher posting' system, where postings are made directly from vouchers to keep ledgers, especially customer accounts, constantly updated. Statement 1 is correct. However, Statement 2 is incorrect; banks place relatively lesser emphasis on traditional books of prime entry like journals compared to the immediate and accurate updating of ledger accounts.

May/June 2022

117. Identify the INCORRECT pair from the following:
(A) Schedule 3 - Deposits
(B) Schedule 10 - Advances
(C) Schedule 8 - Investments
(D) Schedule 12 - Contingent Liabilities

Ans :

(B) Schedule 10 - Advances
The pairing of balance sheet items to their respective schedules must be accurate. Schedule 3 details Deposits, Schedule 8 details Investments, and Schedule 12 details Contingent Liabilities. However, Schedule 10 details Fixed Assets, not Advances. Advances are detailed in Schedule 9, making the pair in option (B) incorrect.

Oct/Nov 2023

118. Which of the following statements is correct regarding the classification of advances in Schedule 9?
(A) 'Unsecured' advances are those not covered by tangible assets or any form of guarantee
(B) Advances are first classified by security, then by type of loan
(C) Advances to the public sector are shown under the 'Priority Sectors' category
(D) Term loans are defined as any loans that are repayable within one year

Ans :

(A) 'Unsecured' advances are those not covered by tangible assets or any form of guarantee
In Schedule 9, Section B classifies advances by security. 'Unsecured' is the residual category for advances that are neither 'Secured by tangible assets' nor 'Covered by bank/Govt. guarantees'. This definition is precise. The other statements are incorrect: classification is by type first; public sector is separate from priority sector; and term loans typically exceed one year.

May/June 2018

119. All of the following are disclosed under Schedule 12 'Contingent Liabilities' EXCEPT:
(A) Claims against the bank not acknowledged as debts
(B) Guarantees given on behalf of constituents
(C) Provision for bad and doubtful debts
(D) Liability for partly paid investments

Ans :

(C) Provision for bad and doubtful debts

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Oct/Nov 2024

5. What type of professional is responsible for developing the software programmes that form the basis of a computer accounting system?
(A) A data entry operator
(B) An accountant
(C) A programmer
(D) A systems analyst

Ans :

(C) A programmer
A computer accounting system operates based on a set of instructions called software programmes. These programmes are developed by a computer software professional known as a programmer. The programmer writes these instructions in a specific computer language, such as COBOL or Foxpro, to create the accounting software that automates the financial processes.

May/June 2010

6. Which category of computers is primarily used in computerised accounting, known for accepting data and converting it into useful results through arithmetic operations?
(A) Analogue Computers
(B) Digital Computers
(C) Hybrid Computers
(D) Mechanical Computers

Ans :

(B) Digital Computers
The text classifies computers into 'Analogue Computers' and 'Digital Computers'. While analogue computers are used in scientific fields for processing continuous data, digital computers are the type used in computerised accounting. They accept data and process it into useful results by performing arithmetic operations based on computer programmes, making them suitable for financial transactions.

Oct/Nov 2016

7. A computer system designed to simulate a guided missile system by combining features of both digital and analogue computers would be classified as what type of computer?
(A) A Supercomputer
(B) A Mainframe Computer
(C) A Digital Computer
(D) A Hybrid Computer

Ans :

(D) A Hybrid Computer
The text specifies that for special purposes, such as simulating a guided missile system, the desirable features of both digital and analogue computers can be combined. The resulting machine is created to leverage the strengths of both types of processing and is referred to as a 'Hybrid Computer', handling both continuous and discrete data.

May/June 2025

8. Which feature of computerised accounting allows for the management of a high volume of transactions, such as 1,000 sales invoices daily, with fewer people and in a shorter time?
(A) Speed
(B) Accuracy
(C) Economy
(D) Report Generation

Ans :

(A) Speed
The text highlights speed as a key feature, explaining that work is done by computers at a very high velocity. It uses the example of accounting for 1,000 daily sales invoices, tracking payments, and managing advances to illustrate how computers can manage these tasks with a small team in a significantly shorter time.

Oct/Nov 2012

9. What feature of computerised accounting ensures that once transactions are correctly fed into the system, calculations are performed without mistakes, allowing a trial balance to be prepared in seconds?
(A) Speed
(B) Versatility
(C) Accuracy
(D) Economy

Ans :

(C) Accuracy
The text emphasizes that unlike people, machines do not make errors once they are programmed to work correctly. This feature is defined as accuracy. The example provided illustrates that while a clerk might take days to find a mistake in a manual trial balance, a computer performs calculations accurately and prepares the trial balance within seconds.

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customer's other accounts are regular
(D) It is treated as an NPA if it remains overdue and unpaid for 90 days

Ans :

(D) It is treated as an NPA if it remains overdue and unpaid for 90 days
Each type of advance has its own NPA criteria. For bills purchased or discounted, the trigger for NPA classification is the bill remaining overdue and unpaid. If this condition persists for a period of 90 days, the asset must be classified as a Non-Performing Asset, and income recognition must shift to a cash basis.

May/June 2021

125. The profit/loss on the sale of investments in the 'Held to Maturity' (HTM) category is transferred to:
(A) The Profit and Loss Account and subsequently to the Capital Reserve Account
(B) The Profit and Loss Account directly with no further appropriation
(C) The General Reserve along with other retained earnings
(D) The Investment Fluctuation Reserve to offset future market losses

Ans :

(A) The Profit and Loss Account and subsequently to the Capital Reserve Account
The treatment of profit or loss on the sale of HTM securities is specific. While the gain or loss is initially routed through the Profit and Loss Account, it is not treated as a normal operating profit. The amount is subsequently appropriated from the P&L account and transferred to the Capital Reserve Account.

Oct/Nov 2006

126. Consider the following statements about Basel III disclosures:
1. Pillar 3 applies at the individual bank level only, not the consolidated group level.
2. Disclosures can be made on the bank's website with a direct link in the published financial statements.

Which of the statements is/are correct?
(A) 1 only
(B) 2 only
(C) Both 1 and 2
(D) Neither 1 nor 2

Ans :

(B) 2 only
Statement 1 is incorrect; Pillar 3 primarily applies at the top consolidated level of the banking group. Statement 2 is correct. The rules provide flexibility, stating that disclosures can be included in published statements or, if operationally inconvenient, disclosed on the bank's website, provided a direct link is given in the financial results.

May/June 2016

127. Which of the following issues is NOT listed as a critical factor to be considered in a bank's Ind AS implementation plan?
(A) Ind AS Technical Requirements
(B) Systems and processes
(C) People-Evaluation of resources and Project management
(D) Customer communication and training

Ans :

(D) Customer communication and training
The text lists several critical issues for the Ind AS implementation plan, including technical requirements, system changes, business impact, resource evaluation (people), and project management. While customer impact is a consideration, direct customer communication and training on accounting standard changes is not listed as a primary critical issue for the internal implementation plan itself.

Oct/Nov 2025

128. Under which schedule would a bank disclose income earned by way of dividends from its subsidiary companies?
(A) Schedule 14: Other Incomes
(B) Schedule 13: Interest Earned
(C) Schedule 15: Interest Expended
(D) Schedule 16: Operating Expenses

Ans :

(A) Schedule 14: Other Incomes
Dividend income is not interest income. Schedule 14 'Other Incomes' has a specific line item for 'Income earned by way of dividends, etc., from subsidiaries Companies and/or joint ventures abroad/in India'. This ensures that such returns on investment are clearly and separately disclosed from the bank's core interest and fee-based incomes.

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Contingent liabilities are potential future obligations. Claims against the bank, guarantees, and liability on partly paid shares all fit this definition. However, provision for bad and doubtful debts is not a contingent liability; it is a current provision for an expected loss on existing assets and is charged to the P&L account.

Oct/Nov 2018

120. A bank's profit and loss ledger contains separate accounts for basic salary, dearness allowance, and other allowances. In the published financial statements, these are grouped under which single head?

(A) Payments to and Provisions for Employees
(B) Other Expenditure
(C) Establishment Expenses
(D) Miscellaneous Expenses

Ans :

(A) Payments to and Provisions for Employees
For internal control, banks maintain detailed expense heads. However, for external reporting, these are consolidated for clarity. All expenses related to employee compensation, such as salary, allowances, and benefits, are aggregated and presented under the single head 'Payments to and Provisions for Employees' in Schedule 16 of the Profit and Loss Account.

May/June 2007

121. A bank's branch adjustment account can appear on:

(A) The assets side of the balance sheet only
(B) The liabilities side of the balance sheet only
(C) Only in the Profit and Loss account
(D) Either the assets side or the liabilities side of the balance sheet

Ans :

(D) Either the assets side or the liabilities side of the balance sheet
The Branch Adjustment Account, or Inter-Office Account, represents the net balance of unreconciled transactions between branches and the head office. If it has a net debit balance, it is shown on the assets side (under Other Assets, Schedule 11). If it has a net credit balance, it is shown on the liabilities side (under Other Liabilities, Schedule 5).

Oct/Nov 2009

122. Which of the following are considered 'Contra Items' in a bank's balance sheet?

1. Bills for Collection
2. Acceptances and Endorsements
3. Statutory Reserve
4. Rebate on Bills Discounted

(A) 1 and 4 only
(B) 2 and 3 only
(C) 1 and 2 only
(D) 3 and 4 only

Ans :

(C) 1 and 2 only
Contra items are those for which a liability entry has a corresponding asset entry, representing a claim on a customer. 'Bills for Collection' and 'Acceptances, Endorsements and Other Obligations' fall into this category. Statutory Reserve is part of shareholders' funds, and Rebate on Bills Discounted is a current liability, neither are contra items.

May/June 2012

123. An advance becomes an NPA when it ceases to generate income. A cash credit account is treated as an NPA if the outstanding amount remains over and above the sanctioned limit or drawing power for more than:

(A) 30 days
(B) 60 days
(C) 90 days
(D) 120 days

Ans :

(C) 90 days
The 'out of order' status for a cash credit or overdraft account is clearly defined. The account is considered an NPA if the outstanding balance continuously remains in excess of the sanctioned limit or the drawing power for a period of more than 90 days. This indicates a sustained irregularity in the account's operation.

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Oct/Nov 2014

124. What is the correct classification for a bill purchased or discounted by a bank that remains overdue and unpaid?

(A) It is treated as a loss asset immediately upon becoming overdue
(B) It is classified as sub-standard after remaining overdue for 30 days
(C) It remains a standard asset as long as the

CHAPTER 18

Core Banking Systems & Accounting in Computerised Environment

Oct/Nov 2018

1. According to the historical context of accounting, what major event spurred the increased use of computers in the maintenance of accounts, especially in advanced countries?
(A) The First World War
(B) The Second World War
(C) The Industrial Revolution
(D) The dot-com bubble

Ans :

(B) The Second World War
The text states that after the Second World War, and with the advent of computers, the use of computers and their peripherals in accounting and financial statement preparation constantly increased. This period marked a significant shift from the older manual methods that used machines like mechanical calculators to more advanced, computer-based systems.

May/June 2021

2. What is the term for an accounting system where functions like capturing business transactions, preparing financial statements, and generating financial reports are performed using a computer?
(A) Computerised Accounting
(B) Manual Accounting
(C) Bookkeeping System
(D) Auditing System

Ans :

(A) Computerised Accounting
The text defines Computerised Accounting as a system where core accounting functions are performed using a computer. These functions include capturing transactions as entries, using those entries to prepare financial statements according to accounting standards, and preparing various financial reports from the available data, all within a computerized environment.

NODIA

Oct/Nov 2005

3. In the context of a computer system, what are the physical components, such as the printer, monitor, keyboard, and disk drive, collectively known as?
(A) Software
(B) Programme
(C) Hardware
(D) Peripherals

Ans :

(C) Hardware
The physical components of which a computer is made up are known as hardware. While components like the printer, video monitor, and keyboard are often referred to as computer peripherals, they are fundamentally part of the overall hardware of the system. The instructions that tell the hardware what to do are called software.

May/June 2013

4. Which term is used to describe a set of instructions that tells a computer what to do, often referred to as a 'programme'?
(A) Hardware
(B) Data
(C) Peripherals
(D) Software

Ans :

(D) Software
The text defines software as the instructions that tell the computer what to do. A set of instructions for solving problems is specifically called a programme, which is a form of software. This is distinct from hardware, which represents the physical components of the computer system that execute these instructions to process information.

(B) ₹2,50,000
(C) ₹4,00,000
(D) ₹5,50,000

Ans :

(D) ₹5,50,000
As of May 1, 2022, the asset has been an NPA for 13 months. It was sub-standard for 12 months and has now been doubtful for 1 month. The unsecured portion is ₹4 lakh (₹10 lakh - ₹6 lakh), requiring a 100% provision (₹4,00,000). The secured portion of ₹6 lakh is doubtful for up to 1 year, requiring a 25% provision (₹1,50,000). Total provision is ₹4,00,000 + ₹1,50,000 = ₹5,50,000.

May/June 2017

101. A bank in India earns a net profit of ₹500 crores for the year. The board wishes to declare a dividend. Based on the rule provided, what is the minimum amount the bank must transfer to its reserve fund before declaring the dividend?
(A) ₹50 crores
(B) ₹125 crores
(C) ₹100 crores
(D) ₹20 crores

Ans :

(C) ₹100 crores
The source specifies a mandatory transfer to the reserve fund before any dividend declaration. The required transfer is twenty per cent (20%) of the net profit for the year. Calculating 20% of the ₹500 crore net profit gives a minimum transfer amount of ₹100 crores (500 × 0.20). This must be done to comply with the regulation.

Oct/Nov 2005

102. A bank has total investments of ₹80,000 crores. It classifies ₹20,000 crores as HTM. The market value of these HTM securities falls by ₹500 crores. Based on the text, what is the impact on the bank's Profit and Loss account?
(A) A loss of ₹500 crores must be booked
(B) There is no immediate impact on the Profit and Loss account
(C) A loss of ₹125 crores (25% of the loss) must be booked
(D) The bank has violated the 25% cap

Ans :

(B) There is no immediate impact on the Profit and Loss account
The source states two key points. First, the bank is within the 25% cap (20,000 is 25% of 80,000). Second, it explicitly mentions that HTM securities need not be marked to market. Therefore, the fall in market value does not require the bank to book a loss in its P&L account. The securities continue to be carried at cost.

May/June 2020

103. A loan was classified as a performing asset and the bank accrued ₹50,000 as interest for the quarter. Before the quarter-end, the account slipped into the NPA category, and the interest was not received. What action should the bank take according to the source?
(A) Ignore the accrual and wait for cash payment
(B) Reclassify the interest as 'Other Income'
(C) Continue to show the ₹50,000 as interest income
(D) Reverse the interest income or make a specific provision for the ₹50,000

Ans :

(D) Reverse the interest income or make a specific provision for the ₹50,000
The source clearly states that if interest on an asset that becomes an NPA has already been recognized on an accrual basis, it must be adjusted. This means the unrealized income should not be part of the bank's profit. The bank must reverse the income entry or make a 100% provision against it to nullify its effect.

Oct/Nov 2015

104. When preparing Schedule 9 'Advances', how should a bank present its term loans according to the provided text?
(A) The total amount including the principal outstanding and any overdue instalments
(B) Only the principal amount outstanding, excluding any overdue instalments
(C) Only the secured portion of the term loans, with unsecured amounts shown elsewhere
(D) As a net figure after deducting the applicable provisions for bad debts

Ans :

(A) The total amount including the principal outstanding and any overdue instalments
The text provides specific instructions for the presentation of term loans in Schedule 9. It explicitly states that "Term loans should be mentioned including overdue instalments."

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May/June 2007

10. The ability of a computerised accounting system to prepare an area-wise list of sales from a large volume of transactions within minutes by giving a few commands is an example of which feature?
(A) Various Informative Reports can be Generated
(B) Accuracy
(C) Economy
(D) Speed

Ans :

(A) Various Informative Reports can be Generated
A key feature of computerised accounting is the ability to generate various statements and reports from the same accounting records, which is difficult in a manual system. The example of creating an area-wise sales list from 500 daily transactions in minutes demonstrates the system's capability to produce diverse and informative reports on demand.

Oct/Nov 2009

11. What is the primary reason that computerised accounting is now considered more economical than manual accounting?
(A) The cost of computers has decreased significantly over the last decade.
(B) Most modern accounting software is now available to businesses for free.
(C) Manual accounting requires more expensive, specialized stationery and ledgers.
(D) The cost of human labour has become costlier due to inflation.

Ans :

(D) The cost of human labour has become costlier due to inflation.
The text explains the economy of computerised accounting by stating that it has become cheaper compared to human labour. The primary driver for this shift is that human labour has become costlier due to inflation, making it more economical to invest in a computer to perform accounting operations than to employ a large workforce.

May/June 2016

12. In a multi-user computerised accounting system, how is the ledger updated?
(A) It is updated manually by an accountant reviewing all entries at the end of the day.
(B) It is updated automatically based on the feeding done by all users.
(C) Each user updates their own separate ledger, which is merged weekly.
(D) The system waits for a scheduled batch process to run overnight to update records.

Ans :

(B) It is updated automatically based on the feeding done by all users.
In a computerised accounting system with multiple users (e.g., on a LAN or WAN), each user handles a specific segment of transactions like sales or purchases. The text states that the ledger gets updated automatically based on the data feeding done by all the users, ensuring a real-time, consolidated view of the accounts.

NODIA

Oct/Nov 2025

13. In the context of computerised accounting, what does the term 'Data' refer to?
(A) The finalized output reports, like the balance sheet, which summarize all transactions.
(B) The set of coded instructions, or software, that tells the hardware how to process information.
(C) Raw facts, observations, or occurrences, like details in a sales invoice, used as input.
(D) The tangible electronic components, like the CPU and monitor, that constitute the computer system.

Ans :

(C) Raw facts, observations, or occurrences, like details in a sales invoice, used as input.
The text defines 'Data' as any facts, observations, assumptions, or occurrences. In an accounting context, this refers to the raw information needed to prepare financial statements. Specific examples given include details from sales invoices like price, sales tax, and date of sale, which are all considered data to be processed by the system.

May/June 2023

14. What is a 'Record' in the terminology of computerised accounting?
(A) A single data item like the price of a product or a specific date.
(B) A compilation of all financial reports generated at year-end.
(C) The entire software program and its modules for accounting.
(D) A group of related data items, such as a sales register of invoices.

(D) Real time on-line banking.
The text explains that with total branch computerisation through Core Banking Solutions, banking becomes "real time on-line banking". This means that whenever a transaction is entered, recorded, verified, and authenticated, all corresponding updates are reflected instantly across the system without any time lag, providing an up-to-the-minute view of accounts.

May/June 2024

32. In a computerised banking environment, what often serves as the basis of the accounting entry after it is fed into the system and validated by a senior executive?
(A) The physical voucher that is prepared for the transaction.
(B) The initial transaction data itself, once it has been validated.
(C) A journal entry that is manually written and approved.
(D) A summary report of transactions generated from the branch.

Ans :

(B) The initial transaction data itself, once it has been validated.
The text states that system software in banks is often designed so that after an error-free feeding of the initial transaction and its validation by a senior executive, this data itself serves as the basis for the accounting entry. In many cases, physical vouchers are not prepared, and the transaction is recorded only on the system.

Oct/Nov 2008

33. How has computerisation improved the management of deposit accounts in banks?
(A) It has made interest calculation a manual, end-of-year process for auditors.
(B) It has automated reminders for renewal and interest calculations.
(C) It requires customers to visit the branch for every single transaction or inquiry.
(D) It has limited the types of deposit schemes that banks are able to offer.

Ans :

(B) It has automated reminders for renewal and interest calculations.
Computerisation has made operating and accounting for deposit accounts easier and more convenient. The text highlights that processes such as sending reminders for renewal, providing interest credit advice, and even the interest calculation itself are now automated. These tasks can be completed within a short span of time, improving efficiency and customer service.

May/June 2006

34. Which of the following banking functions has become faster due to technology, involving fund transfers through systems like RTGS, NEFT, and IMPS?
(A) Lending
(B) Accepting Deposits
(C) Remittances
(D) Operation of safe deposit vaults

Ans :

(C) Remittances
The text specifically mentions that remittances, which involve a bank arranging to remit money to other centres, have become faster due to technology. It explicitly lists RTGS (Real-Time Gross Settlement), NEFT (National Electronic Funds Transfer), and IMPS (Immediate Payment Service) as the methods used for these faster electronic fund transfers between banks.

Oct/Nov 2017

35. What system, operational in some cities, has contributed to the automation of the clearing house functions for cheques?
(A) Cheque Truncation System (CTS)
(B) Automated Teller Machine (ATM) System
(C) Core Banking Solution (CBS)
(D) Standing Instruction System (SIS)

Ans :

(A) Cheque Truncation System (CTS)
While discussing the clearing of cheques, the text notes that the functions of the clearing house are now automated. It specifically mentions that the "Cheque Truncation System is also operational in some cities." This system involves transmitting an electronic image of the cheque, which speeds up the clearing process significantly.

May/June 2008

36. A bank customer has given an instruction to transfer a fixed amount from his salary account to his father's account at another branch every month. How does a computerised system handle such a recurring instruction?
(A) A bank employee must remember to

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Oct/Nov 2010

19. Compared to a manual system, what is the major advantage of a computerised system in terms of generating reports?

(A) It can only generate a single, general-purpose financial statement for all users.
(B) It requires significantly more time to generate any specialized management report.
(C) The cost of preparing specialised management reports is negligible.
(D) It can only generate reports that are pre-defined by the original software vendor.

Ans :

(C) The cost of preparing specialised management reports is negligible.
A major difference is the number and type of reports that can be generated. In manual systems, preparing reports beyond basic financial statements is costly. In contrast, the cost of preparing specialised, customised management reports in computerised systems is negligible, allowing for easy generation of reports tailored to the specific needs of different managers.

May/June 2005

20. Which of the following is an advantage of a computer-based accounting system, especially when the volume of repetitive transactions is large?

(A) It performs functions more rapidly, accurately, and at a lower cost.
(B) It performs functions more slowly but with a greater level of detail.
(C) It operates at a significantly higher cost but is more secure than manual methods.
(D) It requires more manual intervention for each individual transaction.

Ans :

(A) It performs functions more rapidly, accurately, and at a lower cost.
The text lists "Accurate, High Speed and Low Cost of Operation" as a primary advantage. It specifies that a computer-based system performs accounting functions more rapidly and accurately. It also operates at a lower cost, particularly when the volume of repetitive transactions is large, making it more efficient than manual systems in such scenarios.

NODIA

Oct/Nov 2022

21. Which statement best describes the advantage of "Automatic Completion of all Records" in computerised accounting?

(A) The user must manually write subsidiary books, ledgers, and then the financial statements.
(B) The system requires multiple, separate entries for a single transaction to update all records.
(C) Once the initial transaction is fed into the computer, the entire set of accounts gets ready automatically.
(D) The completion of records is automatic but requires a manual review and approval for each step.

Ans :

(C) Once the initial transaction is fed into the computer, the entire set of accounts gets ready automatically.
This advantage means that after the initial feeding of a transaction, the system automatically updates all related records. There is no need to sequentially and manually write subsidiary books, the general ledger, and then prepare financial statements as is required in a manual accounting process. This single-entry update streamlines the entire bookkeeping cycle.

May/June 2018

22. Identify the statement that is NOT an advantage of computerised accounting.

(A) It performs millions of calculations without error, ensuring a high degree of accuracy.
(B) It depends on special programmes that must be developed by costly professional programmers.
(C) It can produce multiple printouts of the same report with various user-defined modifications.
(D) It can easily generate a wide variety of informative reports from the same set of accounting data.

Ans :

(B) It depends on special programmes that must be developed by costly professional programmers.
The requirement for special programmes and professional programmers is listed as a disadvantage of computerised accounting, not an advantage. This is because developing or

with updating applications, troubleshooting, and required technology representatives to be present at each branch for support.

Oct/Nov 2023

41. What technological shift enabled banks to consolidate their databases into a single large database, improving network operations and administration?

(A) The widespread adoption of a decentralised server model for each branch.
(B) The use of multiple older, separate protocols for different communication tasks.
(C) The reliance on individual branch servers for all transaction processing.
(D) The move to a centralised data center architecture.

Ans :

(D) The move to a centralised data center architecture.
The text describes how banks realised the cost benefits of swapping the decentralised model for a centralised data center architecture. This shift allowed them to consolidate their individual branch databases into a single large database. This centralisation using a data centre helped improve and simplify the network from operations, user, and administration perspectives.

May/June 2022

42. In modern banking networks, what type of network is used to handle diverse traffic like data, voice, videoconferencing, and mobile banking?

(A) A potpourri of several older, separate protocols for each traffic type.
(B) A single IP based network.
(C) Separate physical networks for data and telephony traffic.
(D) A decentralised analogue network with limited capacity.

Ans :

(B) A single IP based network.
The text explains that older banking networks were a mix of different protocols and separate networks for different types of traffic. Today, the network has evolved into a unified IP network. This means that a single IP-based network is used for all types of communication, irrespective of whether it is data, voice, or mobile banking traffic.

Oct/Nov 2018

43. What is the primary advantage of core banking applications over traditional localised branch automation systems?

(A) They are only available to customers during specified branch timings.
(B) They require each branch to maintain its own separate customer database.
(C) They provide anywhere, anytime 24 by 7 non-stop services.
(D) They cannot be integrated with any of the bank's in-house applications.

Ans :

(C) They provide anywhere, anytime 24 by 7 non-stop services.
The text contrasts core banking applications with traditional systems by highlighting their continuous availability. It states that core banking applications provide "anywhere, anytime 24 by 7 non-stop services," which is not possible with traditional localised branch automation systems that are available only between specified times, typically normal banking hours.

May/June 2021

44. How do core banking applications help banks in offering a single customer view?

(A) By maintaining separate and distinct databases for each delivery channel.
(B) By restricting a customer's access and transactions to a single home branch.
(C) By providing automation for only front-end services like cash withdrawal.
(D) By integrating the enterprise to existing in-house applications.

Ans :

(D) By integrating the enterprise to existing in-house applications.
The text states that core banking applications help integrate the enterprise with the existing in-house applications to offer a single customer view. This integration ensures that customer information is consistent across all platforms and delivery channels, providing a unified and comprehensive perspective of the customer's relationship with the bank.

Oct/Nov 2005

45. Besides traditional banking products, what other products are core banking applications able to

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Oct/Nov 2011

27. Given the following statements: **Assertion (A) :** The need for specialised programmers can make an efficient computerised accounting system costly.

Reason (R) : Special programmes are required to enable a computer to carry out accounting operations.

(A) Both A and R are true, and R is the correct explanation of A.
(B) Both A and R are true, but R is not the correct explanation of A.
(C) A is true, but R is false.
(D) A is false, but R is true.

Ans :

(A) Both A and R are true, and R is the correct explanation of A.
The assertion that the need for programmers makes the system costly is true. The reason, which states that special programmes are necessary for accounting operations, is also true. The reason correctly explains the assertion because the costliness arises directly from the fact that these essential, special programmes must be written by professional programmers.

May/June 2017

28. Which of the following is listed as a core banking solution software?
(A) QuickBooks
(B) Tally ERP 9
(C) Microsoft Dynamics
(D) Infosys Finacle

Ans :

(D) Infosys Finacle
The text provides a list of various computerised accounting softwares. While Tally, QuickBooks, and Microsoft Dynamics are mentioned as general or specific accounting software, the text explicitly categorizes Infosys Finacle, alongside TCS BaNCS and Flexcube, as a "Core banking solution". This distinction is important for software used specifically in the banking industry.

Oct/Nov 2015

29. Which of the following is NOT a function typically performed by computerised accounting software as listed in the chapter?
(A) Maintenance of statutory books of account.
(B) Generation of reports like area-wise list of sales.
(C) Physical audit of branch inventory.
(D) Conversion of foreign currency transactions into Indian rupees.

Ans :

(C) Physical audit of branch inventory.
The text lists several functions, including maintaining statutory books, generating diverse reports, converting foreign currencies, valuing closing stock, and preparing consolidated financial statements. However, it does not mention performing physical audits of inventory. Software can value stock, but the physical verification or audit remains a separate, manual process not performed by the software itself.

May/June 2020

30. How does accounting software assist an entity with branches all over India and abroad?
(A) It prepares a consolidated trial balance and financial statement for the entity as a whole.
(B) It only maintains the accounts of the head office, requiring branches to report manually.
(C) It requires each branch to use a separate, non-integrated software instance.
(D) It can only handle transactions denominated in Indian rupees, not foreign currencies.

Ans :

(A) It prepares a consolidated trial balance and financial statement for the entity as a whole.
For an entity with numerous branches, the software provides a significant advantage by maintaining the accounts of all branches and the head office in an integrated manner. The text specifically mentions that the software also prepares a consolidated trial balance and financial statement for the entire entity, streamlining the consolidation process.

NODIA

Oct/Nov 2021

31. In modern banking, what is the nature of banking operations when total branch computerisation is implemented?
(A) Batch processing where all transactions are updated at the end of the day.
(B) Manual processing with computer-aided verification for accuracy.
(C) Offline transaction recording with weekly updates to the central server.
(D) Real time on-line banking.

Ans :

acquiring such efficient programmes can be costly. The other options—being error-free, providing multiple printouts, and generating various reports—are all listed as distinct advantages of using a computerised system.

Oct/Nov 2007

23. What is a primary disadvantage associated with the staffing requirements for computerised accounting?

(A) It requires a large and expanded number of people dedicated solely to data entry tasks.
(B) It completely reduces the need for any underlying accounting knowledge among system users.
(C) It fully eliminates the need for any professional supervision or oversight of the system.
(D) It requires technically qualified staff, which in turn increases initial training and hiring costs.

Ans :

(D) It requires technically qualified staff, which in turn increases initial training and hiring costs.
A key disadvantage is the need for qualified staff. The text states that only a technically qualified person can operate a computer for accounting. This necessitates initial training for existing staff or hiring new staff, which increases staff costs, especially during the transition from a manual to a computerised accounting system.

May/June 2014

24. Which of the following is a disadvantage related to the physical components of a computerised accounting system?

(A) Peripherals like printers and storage devices can be costly.
(B) Computers do not require any special or expensive stationery.
(C) The system can operate effectively without any peripheral devices.
(D) Traditional books of account are more expensive than computer peripherals.

Ans :

(A) Peripherals like printers and storage devices can be costly.
The text lists "Costly Computer Peripherals and Stationery" as a disadvantage. A computer system requires various peripherals for storage (hard disks, servers), output (printers), and other functions. These components, along with special stationery, can be costly when compared to the materials needed for traditional books of account, adding to the overall expense.

Oct/Nov 2019

25. Why is regular data back-up a critical requirement in computerised accounting?

(A) To free up primary storage space on the main computer for new transactions.
(B) To comply with international accounting standards for data archiving.
(C) To guard against possible loss of data due to inadvertence or system failure.
(D) To speed up the computer's overall processing power and daily performance.

Ans :

(C) To guard against possible loss of data due to inadvertence or system failure.
A significant disadvantage of computerised systems is the risk of data loss. The text explicitly states that regular back-ups on devices like hard disks, magnetic tapes, or servers are required to guard against this. It is difficult to retrieve data that has been lost from a computer due to inadvertence or other issues.

May/June 2009

26. What is a "computer virus" in the context of computerised accounting risks?

(A) A hardware malfunction that causes the system to corrupt stored data.
(B) A mischievous computer software that damages or destroys data.
(C) A type of common user error made during high-volume data entry.
(D) A security feature that protects the system from unauthorized network access.

Ans :

(B) A mischievous computer software that damages or destroys data.
The text defines a computer virus as a mischievous computer software. It is a significant risk because it can damage data inside a computer and may even destroy the entire data set, including any data that has been kept in a back-up. This highlights the vulnerability of digital data to malicious software attacks.

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manually execute the transfer each month.
(B) The instruction is fed into the system to be performed automatically each month.
(C) The customer must provide a new, separate instruction for the transfer every month.
(D) The system sends a monthly reminder to the bank manager to approve the transfer.

Ans :

(B) The instruction is fed into the system to be performed automatically each month.
This scenario describes a standing instruction. The text explains that for such recurring instructions, the bank can feed the details into their computer system to perform them automatically. This eliminates the need for bank staff to manually remember and execute the instruction each time, ensuring timely and accurate execution of the customer's request.

Oct/Nov 2013

37. What principle allows a customer with an account in one branch to deposit or withdraw money from any other on-line branch of the same bank?
(A) Automated Banking
(B) Centralised Banking
(C) Decentralised Banking
(D) Manual Banking

Ans :

(B) Centralised Banking
The text defines centralised banking as the principle where all branches of a bank are linked to each other on-line. This connectivity makes it possible for banks to offer customers the facility of banking at any branch or outlet of the bank, allowing them to deposit, withdraw, or make enquiries from different locations.

May/June 2015

38. What technology is primarily associated with the concept of automated banking, providing 24/7 services like cash disbursal and balance enquiry?
(A) Automated Teller Machines (ATMs)
(B) Cheque Truncation System (CTS)
(C) Real-Time Gross Settlement (RTGS)
(D) Core Banking Solutions (CBS)

Ans :

(A) Automated Teller Machines (ATMs)
The concept of automated banking is identified as a result of computerisation and technological innovation, with Automated Teller Machines (ATMs) being the prime example. ATMs are capable of performing various banking tasks like accepting cash/cheques, disbursing cash, and balance enquiries on a 24-hour, 365-day basis without human intervention.

Oct/Nov 2020

39. What are the three core areas of focus for banks in the modern competitive environment that technology helps to address?
(A) Increasing the number of physical branches, hiring more staff, and manual processing.
(B) Reducing working hours, closing unprofitable branches, and increasing service charges.
(C) Meeting customer service expectations, cutting costs, and managing competition.
(D) Focusing only on corporate clients, government business, and international trade.

Ans :

(C) Meeting customer service expectations, cutting costs, and managing competition.
The text explicitly states that banks are focused on three areas: meeting customer's service expectations, cutting operational costs, and managing competition. Technology, particularly automation and core banking applications, is presented as a key enabler for banks to achieve these strategic objectives and remain competitive in the financial services sector.

May/June 2011

40. What was a major problem associated with the decentralised network infrastructure used in the early days of banking technology?
(A) Lack of coordination and problems with updating applications across branches.
(B) Low capital expenditure and minimal overall resource requirements.
(C) A single central control point that managed all branch operations.
(D) Instantaneous database updates across all branches and channels.

Ans :

(A) Lack of coordination and problems with updating applications across branches.
The decentralised model, where each branch had its own server and applications, suffered from several problems. The text highlights that in this model, there was no coordination or a single central control point. This led to issues

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Ans :

(D) A group of related data items, such as a sales register of invoices.
A 'Record' is defined as a group of data items that are related to an object of data processing. The example provided is that a sales register, which contains multiple data points about various sales invoices, can be called a record of sales invoices. It represents a structured collection of related data.

Oct/Nov 2014

15. A payroll file containing information for 1,000 employees of an entity is an example of which computerised accounting term?
(A) Data File or File
(B) Data
(C) Record
(D) System

Ans :

(A) Data File or File
A 'Data File' or 'File' is described as a compilation of related data records maintained in a pre-arranged order, similar to a manual file. The text gives the specific example of a payroll file for 1,000 employees of an entity to illustrate this concept, as it contains multiple related records (one for each employee).

May/June 2012

16. In a computerised accounting 'System', which of the following are considered its core components?
(A) The persons involved, the books of account, and the physical ledgers.
(B) The computer machine, the software programme, and computer peripherals.
(C) Only the accounting entries and their corresponding source documents.
(D) The final trial balance, financial statements, and management reports.

Ans :

(B) The computer machine, the software programme, and computer peripherals.
The term 'System' refers to the various components that process data to produce results. In a computerised accounting system, these components are identified as the computer machine itself, the software programme containing the instructions, and computer peripherals like the keyboard and monitor, which facilitate input and output for the entire process.

Oct/Nov 2006

17. What is a primary difference between manual and computerised accounting regarding the 'trail of events'?
(A) The audit trail is significantly easier to establish in most computerised systems.
(B) Tracing a document to its entry is more difficult in computerised systems.
(C) Manual systems do not possess a clear or traceable audit trail.
(D) Computerised systems completely eliminate the need for source documents.

Ans :

(B) Tracing a document to its entry is more difficult in computerised systems.
A key difference highlighted is the difficulty in establishing an acceptable audit trail in computerised systems. This is because data storage and arithmetic manipulations are internal and not physically visible. Tracing a source document through its journal entry to its final place in the ledger becomes more challenging compared to the clear, physical path in manual accounting.

May/June 2019

18. Why is the integrity of accounting data a significant concern in computerised systems?
(A) Because computerised data records are subject to a risk of manipulation.
(B) Because data is stored physically and can be easily lost or misplaced.
(C) Because computers frequently make calculation errors in complex operations.
(D) Because data cannot be effectively backed up in a computerised system.

Ans :

(A) Because computerised data records are subject to a risk of manipulation.
The text points out that the integrity of accounting data within a computerised database is a real concern for both makers and users of financial statements. This is because the data records in a computer are not physically visible and are therefore subject to a higher risk of manipulation, which can lead to computer fraud.

NODIA

support, allowing banks to reinvent themselves as marketing agencies?
(A) Products like life insurance, RBI bonds, and credit cards.
(B) Only traditional savings and current accounts.
(C) Only basic fixed and recurring deposits.
(D) Only agricultural and small business loan products.

Ans :

(A) Products like life insurance, RBI bonds, and credit cards.
The text mentions that banks are reinventing themselves as marketing agencies by selling a wider range of products. It explicitly states that core banking applications are able to support the sale of products like life insurance, RBI bonds, and credit cards, expanding the bank's role beyond purely traditional deposit and loan services.

May/June 2013

46. What management practice and technology tool is crucial for banks to improve service levels and treat customers right in a hypercompetitive environment?
(A) Enterprise Resource Planning (ERP)
(B) Customer Relationship Management (CRM)
(C) Supply Chain Management (SCM)
(D) Total Quality Management (TQM)

Ans :

(B) Customer Relationship Management (CRM)
The text identifies managing customers as a main issue and emphasizes that customer service levels are what matter. It states that this is where Customer Relationship Management (CRM) practices and software play an important role. CRM is presented as a tool that helps banks to know, emote, and relate with their customers effectively.

Oct/Nov 2024

47. Which of the following is NOT listed as an aspect of information security covered by a core banking solution?
(A) Core Bank Product Build
(B) Core Bank Customer Management and Customer Overview
(C) Core Bank Branch Physical Security
(D) Core Bank Financial Institution Infrastructure

Ans :

(C) Core Bank Branch Physical Security
The text provides a specific list of "Core Bank Components". This list includes Financial Institution Infrastructure, Product Build, Customer Management, Account Administration, Payments, and Management Information. Branch Physical Security, while important for a bank, is not listed as one of these specific integrated software components of a core banking system.

May/June 2010

48. How does core banking support an organization's Customer Relationship Management (CRM) strategy?
(A) By providing a robust database and efficient customer administration.
(B) By providing a separate, non-integrated marketing database for campaigns.
(C) By strictly limiting customer data access to senior management and auditors.
(D) By outsourcing all customer-facing interactions to an external third-party vendor.

Ans :

(A) By providing a robust database and efficient customer administration.
A significant benefit of core banking is its ability to enable an organization's CRM strategy. It achieves this by providing a robust, centralized operational customer database and an efficient customer administration system. This forms the technological foundation upon which effective customer relationship management practices can be built and executed across the bank.

Oct/Nov 2016

49. The ability to create flexible financial products in line with prevailing market conditions is supported by which core banking component?
(A) Core Bank Payments
(B) Core Bank Management Information
(C) Core Bank Product Build
(D) Core Bank Account Administration

Ans :

(C) Core Bank Product Build
The text highlights that core banking supports portfolio growth with a "fast-track Product Build component". This specific component is designed to create flexible financial products quickly. This

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capability allows the bank to respond rapidly to changing market conditions by developing and launching new products, a benefit termed as "speed to market".

May/June 2025

50. Which of the following is a stated benefit of core banking solutions?
(A) Facilitation of increased productivity and reduction of errors.
(B) Increased errors due to the automation of complex calculations.
(C) Support for single-currency and single-language operations only.
(D) Restricted operational efficiency with standard 9-to-5 operations.

Ans :

(A) Facilitation of increased productivity and reduction of errors.
The text lists several benefits of core banking. Among them is the facilitation of increased productivity and reduction of errors. This is achieved through components that automate complex calculations, such as those for fees and interest rates, thereby minimizing manual mistakes and improving overall operational efficiency for the bank's staff.

Oct/Nov 2012

51. Core banking solutions provide support for multi-bank and single-bank operations. What strategic activities does this capability primarily support?
(A) Daily cash management and branch-level reconciliation.
(B) Employee training and professional development programs.
(C) Regulatory reporting to the central bank and other authorities.
(D) Mergers and acquisitions and other branding strategies.

Ans :

(D) Mergers and acquisitions and other branding strategies.
The text explicitly mentions that providing full multi-bank and single-bank operations, including multi-language support, is a benefit that serves to support "mergers and acquisitions and other branding strategies." This flexibility in the system's architecture allows different banking entities to be integrated or managed separately on the same platform.

NODIA

May/June 2007

52. What is the role of the centralised data centre in the technical architecture of Core Banking Solutions?
(A) It acts as a local backup server, used only when individual branch servers fail.
(B) It is the 'Hub' where a powerful server is installed, connected to all branch servers.
(C) It is a customer-facing terminal used for self-service banking operations.
(D) It only stores non-transactional data like employee records and marketing materials.

Ans :

(B) It is the 'Hub' where a powerful server is installed, connected to all branch servers.
The technical architecture described is a hub-and-spoke model. A powerful server is installed at the centralised data centre, referred to as the 'Hub'. Each branch has its own server, which in turn connects to this central server. This architecture ensures that all data is processed and stored centrally, enabling system-wide access.

Oct/Nov 2009

53. In the system layers of core banking architecture, which layer is responsible for the interface between the front-end and the operating system?
(A) Presentation layer
(B) Application layer
(C) Database layer
(D) Delivery layer

Ans :

(D) Delivery layer
The text outlines four system layers. It explicitly states that the Delivery layer's function is to act as the "Interface between front-end and operating system." This layer manages the communication and data flow between the user-facing presentation layer and the underlying system environment, ensuring that requests are correctly processed.

May/June 2016

54. Which layer in the core banking architecture is driven by system triggers, parameters, and environment settings?
(A) Application layer
(B) Presentation layer
(C) Database layer
(D) Delivery layer

Ans :

(A) Application layer

The Application layer is described as being "Driven by system triggers, parameters and environment settings." This is the core logic layer where the actual business rules, transaction processing logic, and functionalities of the banking application reside and are executed based on various predefined conditions and inputs from other layers.

Oct/Nov 2025

55. What is the main purpose of the 'secondary update method' in core banking transaction processing?

(A) For posting external transaction records like salary files received electronically.
(B) For customer-related operations like deposits and withdrawals initiated at the branch.
(C) For tasks like daily interest updating and generating end-of-day statistical reports.
(D) For creating new customer accounts and information files (CIF) online.

Ans :

(A) For posting external transaction records like salary files received electronically.

The text distinguishes between different update methods. It specifies that the 'secondary update method' is mainly used for posting external transaction records. The example given is salary files that are received electronically or through media like tape or disc, which need to be posted to multiple customer accounts in the system.

May/June 2023

56. Which transaction processing method in core banking is primarily used for tasks like daily interest updating and generating statistical reports?

(A) Primary update method
(B) Batch processing
(C) Online processing
(D) Secondary update method

Ans :

(B) Batch processing

The text states that 'Batch processing is mainly used for daily interest updating and statistical reports'. These are tasks that are typically not time-critical to be processed individually in real-time. Instead, they are grouped together and processed as a batch, often during off-peak hours to optimize system resources.

Oct/Nov 2014

57. Based on the following source text, what is the 'maker-checker' functionality?

"The maker checker functionality defined in brief, is that when a teller or user (Clerical/Cashier level) initiates a transaction, the transaction has to be authorised by a supervisory official if the transaction exceeds the authority of the teller who initiates the transaction. This is managed in the system through queues."

(A) A redundant entry process where two tellers must independently input the same transaction to ensure validity.
(B) A dual-control process requiring a supervisor to authorize transactions beyond a teller's limit.
(C) An automated system feature that uses image recognition to automatically verify a customer's signature on file.
(D) A simplified functionality where the maker and checker roles are combined for transactions below a certain value.

Ans :

(B) A dual-control process requiring a supervisor to authorize transactions beyond a teller's limit.

The provided text explicitly defines the maker-checker functionality. It states that when a teller (the maker) initiates a transaction that exceeds their authority, it must be authorized by a supervisory official (the checker). This dual control mechanism is managed through a queue system to ensure proper oversight and security for certain transactions.

May/June 2012

58. A teller at a bank using the TCS BaNCS system initiates a cash withdrawal for a customer. The transaction amount is within the teller's authorized limit. What is the most likely outcome?

(A) The transaction hits the host, is validated, and the account is updated without supervisory authorization.
(B) The transaction is automatically sent to a supervisor's queue for mandatory authorization.
(C) The transaction is immediately rejected with an error message due to a system policy.

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(D) It synchronises data in real time, allowing users to start on one channel and finish on another.

Ans :

(D) It synchronises data in real time, allowing users to start on one channel and finish on another.
The text highlights the benefit of data synchronization in real time across all channels. It gives the specific example of a user starting the onboarding process on one channel (e.g., mobile app) and finishing it on another (e.g., website) "without having to provide the same information twice," which simplifies the process and enhances customer experience.

Oct/Nov 2018

85. What defines a 'Neo-bank'?
(A) A bank that operates without a physical branch network, conducting business entirely online.
(B) A traditional bank that has recently developed a strong online presence and mobile app.
(C) A specialized financial institution that only offers commercial loan products.
(D) A type of bank that exclusively serves high-net-worth corporate clients.

Ans :

(A) A bank that operates without a physical branch network, conducting business entirely online.
The text defines a neo-bank as "a bank that operates without a physical branch network, that is, the banking business is conducted entirely online." This digital-only model is the key characteristic that distinguishes neo-banks from traditional banks, even those that offer extensive digital services but still maintain physical branches.

May/June 2021

86. Who is the primary target audience for neo-banks?
(A) Elderly customers who prefer the familiarity of in-person banking services.
(B) Tech-savvy people who prefer managing their money through mobile phones or tablets.
(C) Large corporations requiring complex international trade finance services.
(D) Customers who do not have reliable access to the internet or a smartphone.

Ans :

(B) Tech-savvy people who prefer managing their money through mobile phones or tablets.
The text states that the concept of neo-banks has become "appealing to tech-savvy people who prefer managing their money through mobile phones or tablets." These users are comfortable with digital interfaces and value the convenience and simplicity offered by an entirely online banking experience, making them the ideal customer base for neo-banks.

Oct/Nov 2005

87. Which of the following is listed as an advantage of neo-banking?
(A) A complex, multi-stage account opening procedure requiring branch visits.
(B) Higher operational costs which are then passed on to customers as higher fees.
(C) A simple and user-friendly interface.
(D) The mandatory requirement to visit a physical location for identity verification.

Ans :

(C) A simple and user-friendly interface.
The text lists several advantages of neo-banking, which include a simple account opening procedure, lower costs, and "a simple and user-friendly interface." This focus on user experience is a key selling point, designed to appeal to the tech-savvy demographic that values intuitive and easy-to-navigate digital financial tools.

May/June 2013

88. Evaluate the following statements:
Statement I : In a manual accounting system, the cost of preparing specialised reports is high.
Statement II : In a computerised system, a large number of customised reports can be easily generated at a negligible cost.
(A) Only Statement I is correct.
(B) Only Statement II is correct.
(C) Both Statement I and Statement II are correct.
(D) Both Statement I and Statement II are incorrect.

Ans :

(C) Both Statement I and Statement II are correct.
The text explicitly contrasts manual and computerised systems on report generation. It states that in a manual system, the cost of preparing reports beyond the basic financial

NODIA

Oct/Nov 2022

63. As per the standard practices for PC and laptop usage in a bank, what is a key responsibility of the users regarding their desktops?

(A) To share their login credentials with team members to improve overall efficiency.
(B) To take adequate measures to restrict physical and logical access.
(C) To install any software they find useful for their work without prior approval.
(D) To disable the system's anti-virus software to improve daily performance.

Ans :

(B) To take adequate measures to restrict physical and logical access.
The first point under standard practices states that "Users are responsible for the security of their desktops and should take adequate measures to restrict physical and logical access to their desktops." This places the primary responsibility on the individual employee to safeguard the machine they use from any unauthorized access, both physically and through the network.

May/June 2018

64. What does "secure configuration" of hardware/ software in a bank entail, according to the provided text?

(A) Disabling all security features to ensure maximum compatibility with older systems.
(B) Allowing users to change any hardware or software settings as they see fit.
(C) Installing software directly from the internet without vetting by any authority.
(D) Enabling auto anti-virus updates, firewalls, and enforcing passwords.

Ans :

(D) Enabling auto anti-virus updates, firewalls, and enforcing passwords.
The text defines secure configuration with specific examples. It "shall mean enabling auto anti-virus updates, enabling firewalls (where the operating system allows the same), enforcing passwords, disabling macros by default, patch management (software upgrades) or any other such configuration standards." These measures are designed to harden the system against security threats.

Oct/Nov 2007

65. An employee at a bank wants to install an additional software application on their desktop, believing it will help with their work. What is the correct procedure they must follow?

(A) The software should be installed only after being vetted by the competent authority.
(B) Install the software immediately as long as it is for official business purposes.
(C) Get verbal approval from their immediate supervisor and proceed with the installation.
(D) Ask a colleague from the IT department to install it for them unofficially.

Ans :

(A) The software should be installed only after being vetted by the competent authority.
The policy is very clear on this matter. The text states, "Users should not install any software or applications... that is not authorised or not essential to bank's business." It further specifies that if additional software is required, it should be installed "only after getting it vetted by the competent authority."

May/June 2014

66. Why are users generally prohibited from connecting their own routers or dongles to their machines to access the internet?

(A) Because doing so can significantly slow down the bank's official network for everyone.
(B) Because it exposes the entire network to several risks.
(C) Because it is a direct violation of the software license agreements with vendors.
(D) Because the additional devices consume too much electricity from the power grid.

Ans :

(B) Because it exposes the entire network to several risks.
The text provides a clear security reason for this restriction. It states that accessing external networks, including the internet, using unauthorized devices like modems (or routers/ dongles) "exposes the entire network to several risks." This creates an unsecured entry point that bypasses the bank's established security controls, endangering the whole system.

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(D) The system requires a second teller from the same branch to co-authorize the transaction.

Ans :

(A) The transaction hits the host, is validated, and the account is updated without supervisory authorization.
The maker-checker logic described applies when a transaction exceeds the teller's authority. Since this transaction is within the authorized limit, it does not need to go to a supervisor's queue. The system would validate the details (account number, balance, etc.) and, upon successful validation, update the account directly.

Oct/Nov 2006

59. In the TCS BaNCS transaction flow, what happens if a transaction initiated at the branch level does not meet a condition set at the product level?
(A) The transaction is manually corrected by the supervisor and then re-processed.
(B) The transaction is put on hold for end-of-day batch processing and review.
(C) The transaction is rejected, the account is not updated, and an error message is sent back.
(D) The system automatically overrides the condition and processes the transaction anyway.

Ans :

(C) The transaction is rejected, the account is not updated, and an error message is sent back.
The text clearly states the outcome for a non-compliant transaction. If the transaction does not meet any of the conditions set at the product level, or exceeds authority, it "will be rejected and the account will not be updated and an error message with a brief description will be sent back to the branch."

May/June 2019

60. What type of processing solution are popular Core Banking Systems (CBS) like Infosys Finacle, TCS BaNCS, and Oracle Flexcube based on?
(A) Online Transaction Processing
(B) Manual Transaction Processing
(C) Batch Transaction Processing
(D) Offline Transaction Processing

Ans :

(A) Online Transaction Processing
The text explicitly categorizes core banking solutions under the heading "The Accounting of Transactions". It states that "Core banking solutions are Online Transaction Processing Solutions used in banking." This means they process transactions in real-time as they occur, immediately debiting and crediting the affected accounts, which is a hallmark of modern CBS platforms.

Oct/Nov 2010

61. According to the chapter, who holds the responsibility for protecting the information assets of a bank and maintaining data security?
(A) Only the dedicated IT department and its security specialists.
(B) Only the senior management and the board of directors.
(C) Only the external auditors and government regulators.
(D) Every employee of the organisation.

Ans :

(D) Every employee of the organisation.
The section on Information Security begins with a definitive statement: "Information security is the responsibility of every employee of an organisation." It emphasizes that all employees are responsible for protecting the bank's information assets and maintaining data security by adhering to the bank's established policies, procedures, standards, and practices.

May/June 2005

62. Which of the following is NOT listed as an aspect of information security covered by a core banking solution?
(A) Logical Access Control
(B) Customer satisfaction surveys.
(C) Password management
(D) Malicious software

Ans :

(B) Customer satisfaction surveys.
The text provides a comprehensive list of areas covered by information systems security. This list includes technical and procedural controls like logical access control, password management, and protection against malicious software. Customer satisfaction surveys, while a business metric, are not a component of the information security framework described in this context.

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(C) A unique phrase that is easy for the user to remember but hard for others to guess.
(D) Common words found in an English dictionary.

Ans :

(D) Common words found in an English dictionary.
The guidelines for password construction explicitly state that "Common words found in English dictionary should not be used." Such words are susceptible to dictionary attacks, where an attacker systematically tries all words in a dictionary to guess the password. The other options describe characteristics of strong, recommended passwords.

May/June 2020

72. Which of the following is an example of a weak password construction practice mentioned in the text?
(A) Using a strong mix of capital letters, lowercase letters, and special characters.
(B) Using word or number patterns like 'qwerty' or '123321'.
(C) Taking a known phrase and converting it with symbols (e.g., 'To be or not to be' -> '2b|!2b').
(D) Creating a password with a minimum length of eight characters or more.

Ans :

(B) Using word or number patterns like 'qwerty' or '123321'.
The text provides specific examples of what to avoid in password construction. It explicitly warns against using "Word or number patterns like aaabbb, qwerty, zyxwvuts, 123321, etc." These patterns are common, easy to guess, and are considered a hallmark of a weak password, making the user's account vulnerable to being compromised.

Oct/Nov 2021

73. What is the recommended course of action if a password needs to be shared under unavoidable circumstances?
(A) The password should be written down and given to the other person in a sealed envelope.
(B) The password should be used by both individuals for at least one month for consistency.
(C) The password should be changed at the next log in by the owner.
(D) A request should be sent to the IT department to create a new shared password.

Ans :

(C) The password should be changed at the next log in by the owner.
The password protection policy states that passwords should not be shared. However, it provides a contingency: "If the password needs to be shared under unavoidable circumstances, care should be taken to change it at the next log in by the owner of the password." This minimizes the window of vulnerability after the shared access.

May/June 2024

74. An employee, User A, notices another employee, User B, watching them as they type their password. According to the password protection guidelines, what should User A do?
(A) Ignore User B as they are a trusted colleague from the same department.
(B) Report User B to the Human Resources department for professional misconduct.
(C) Continue entering the password carefully but make a note to change it later in the day.
(D) Ensure nobody is watching when entering a password into the system.

Ans :

(D) Ensure nobody is watching when entering a password into the system.
This scenario directly relates to the explicit guideline provided in the text. It states, "Users should ensure that nobody is watching when they are entering password into the system." This is a proactive security measure to prevent shoulder surfing. The policy also states users should not watch others entering their passwords, making both actions improper.

Oct/Nov 2008

75. Under which of the following circumstances is a user NOT required to change their password?
(A) After successfully logging in without any issues.
(B) At least once in thirty days, as per the periodic interval policy.
(C) When a change is enforced by the system's security policy.
(D) After it has been shared with someone else, even under unavoidable circumstances.

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easily and quickly," indicating comprehensive automation of the lending cycle.

Oct/Nov 2012

93. Based on the following source text, which benefit is directly related to the bank's ability to introduce new financial products quickly?

"• Enable the organisation's Customer Relationship Management (CRM) strategy... • Provide cost savings and improved customer service... • Support portfolio growth with a fast-track Product Build component... • Deliver speed to market in terms of product development..."

(A) Enabling the CRM strategy
(B) Providing cost savings
(C) Delivering speed to market
(D) Improving customer service

Ans :

(C) Delivering speed to market
The source text links the fast-track Product Build component to supporting portfolio growth. It further clarifies this by stating a benefit is to "Deliver speed to market in terms of product development." This specific phrase directly refers to the bank's ability to develop and launch new products rapidly in response to market demands.

May/June 2007

94. Based on the following source text, what is the primary reason given for the restriction on connecting personal routers?

"Users should not connect routers or dongles to connect their machines to internet unless and otherwise approved by the appropriate authority. Accessing external networks, including internet, using modems, exposes the entire network to several risks."

(A) It consumes an excessive amount of the bank's official network bandwidth.
(B) It can lead to critical hardware incompatibility issues with bank equipment.
(C) It introduces significant security vulnerabilities to the bank's network.
(D) It is a direct violation of the bank's internet service provider's usage policy.

Ans :

(C) It introduces significant security vulnerabilities to the bank's network.
The provided text explicitly states the rationale behind the rule. It says that connecting such devices to access external networks "exposes the entire network to several risks." This indicates that the primary concern is not performance or policy, but the significant security threat that such an unauthorized connection poses to the bank's internal network.

Oct/Nov 2009

95. Based on the description of password construction guidelines, which of the following would be considered a weak password?

"Own name... should not be used. Personal information like date-of-birth... should not be used. Common words found in English dictionary should not be used. Word or number patterns like aaabbb, qwerty... should not be used."

(A) P@ssw0rd1
(B) MyBnk@2024!
(C) Jsmith1990
(D) 1s3cr3t!

Ans :

(A) P@ssw0rd1
The password 'P@ssw0rd1' is a classic example of a weak password that tries to appear strong. It is a common dictionary word ('password') with simple substitutions ('a' for '@', 'o' for '0') and a digit appended. The guidelines warn against using common dictionary words, and this is a thinly disguised version of one, making it easy to guess.

May/June 2016

96. Based on the following source text, what key capability of an omni-channel platform does the example illustrate?

"An omni-channel banking platform synchronises data in real time across all channels. For example, users can start the onboarding process on one channel and finish it on another without having to provide the same information twice."

(A) Real-time data synchronisation
(B) Enhanced marketing performance
(C) Increased customer retention
(D) Simplified onboarding processes

Ans :

(A) Real-time data synchronisation
While simplified onboarding is the result, the underlying capability being demonstrated is real-time data synchronisation. The text explicitly states that the platform "synchronises data in real time across all channels," and then uses the onboarding example to illustrate what this

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May/June 2015

80. What does 'E-commerce' refer to?
(A) Electronic Commerce, which is the buying and selling of goods and services on the Web.
(B) The process of sending and receiving electronic messages through the internet as mail.
(C) The main index page that serves as the entry point for an organization's website.
(D) The global inter-connection of computer networks and servers across the globe.

Ans :

(A) Electronic Commerce, which is the buying and selling of goods and services on the Web.
The text defines E-commerce as "Electronic Commerce, i.e. buying and selling on the Web." It is described as a way of enabling business over the internet, where products and services can be offered through sites. This involves transactions, often using credit cards, making security and secrecy crucial components for a trustworthy solution.

Oct/Nov 2020

81. With the advent of the internet and WWW, a modern bank is expected to be 'The Convenience Bank'. What does this concept primarily imply?
(A) Having a working schedule of 365 days a year and 24 hours a day.
(B) Having more physical branches located in remote rural areas.
(C) Offering significantly higher interest rates than all of its competitors.
(D) Providing customer services exclusively through telephone banking.

Ans :

(A) Having a working schedule of 365 days a year and 24 hours a day.
The concept of 'The Convenience Bank' is linked directly to the capabilities enabled by technology. The text explains that a modern bank is now expected to have a working schedule of 365 days a year and 24 hours a day. This round-the-clock availability, moving beyond the traditional five-and-a-half-day week, is a core aspect of this new expectation.

May/June 2011

82. What facility allows a customer to perform 'Round the Clock' banking, primarily through the use of an automated teller machine (ATM) card?
(A) Home-Banking
(B) ATM Banking
(C) Dial 'n' bank
(D) Sunday banking

Ans :

(B) ATM Banking
The text directly links the facility of banking 'Round the Clock' with the Automated Teller Machine (ATM) card. While Home-Banking and other services contribute to overall convenience, the specific phrase 'Round the Clock' is used in the context of ATM services that are available 24/7 for transactions like cash withdrawal.

Oct/Nov 2023

83. What is the core principle of Omni-channel Banking?
(A) Providing a different and unique set of services on each different channel.
(B) Requiring customers to complete a process on the same channel where it was started.
(C) Providing the same set of services to customers across all channels, digital or physical.
(D) Focusing exclusively on digital channels like mobile apps and websites, phasing out branches.

Ans :

(C) Providing the same set of services to customers across all channels, digital or physical.
The definition provided states that "Omni-channel banking provides the same set of services to customers across all channels, whether digital or physical." The key idea is consistency and integration, allowing users to interact with the bank seamlessly through a website, mobile app, branch, or call centre for the same services.

May/June 2022

84. How does an omni-channel banking platform improve the customer onboarding process?
(A) It requires all customers to visit a physical branch to complete the onboarding process.
(B) It simplifies the onboarding process by removing the need for any identity verification.
(C) It makes the onboarding process longer by requiring information to be entered on each channel.

Oct/Nov 2019

67. According to the password policy described, what is the minimum length for a password and how often should it be changed?

(A) 6 characters, changed at least once every six months.

(B) 10 characters, changed only when a compromise is suspected.

(C) 8 characters, changed at least once every year.

(D) 8 characters, changed at least once every month.

Ans :

(D) 8 characters, changed at least once every month.

The text specifies the password construction and change policy clearly. It states, "The passwords selected should be of a minimum eight characters with a combination of alphabets and digits." It further adds, "The passwords should be changed at periodic intervals at least once every month," controlled by the Password Security Policy.

May/June 2009

68. Which of the following is a recommended protection measure to prevent unauthorised access when a user leaves their desktop unattended for a short duration?

(A) Enable the screen saver with password protection.

(B) Log out of all applications and network connections.

(C) Shut down the computer completely to clear the memory.

(D) Ask a nearby colleague to watch the desktop until they return.

Ans :

(A) Enable the screen saver with password protection.

The text provides distinct measures for different situations. While logging out is recommended for leaving the desktop unattended "at any time," for "short durations," the specific measure is to "enable the screen saver with password protection." This allows the user's session to remain active while securing the terminal from immediate unauthorized use.

Oct/Nov 2011

69. In the context of core banking users, what specific care should be taken to prevent unauthorized actions?

(A) To share terminals with other users to speed up customer service during peak hours.

(B) To disable folder sharing only at the end of the day before leaving the office.

(C) Not to leave terminals in the middle of a transaction.

(D) To write down passwords and keep them in a secure location near the terminal.

Ans :

(C) Not to leave terminals in the middle of a transaction.

A specific precaution for core banking users is mentioned: "care should be taken not to leave the terminals in the middle of a transaction." Leaving a terminal mid-transaction could allow an unauthorized person to complete, alter, or cancel the transaction, leading to financial loss or fraud. This is a critical operational security measure.

May/June 2017

70. According to the Password Management Policy, who is responsible for all activities originating from an employee's computer account?

(A) The employee (User)

(B) The IT department

(C) The branch manager

(D) The system administrator

Ans :

(A) The employee (User)

The policy begins by establishing individual accountability. It states, "Employees (Users) are responsible for all activities originating from their computer accounts." This principle underscores the importance of users protecting their credentials, as they will be held accountable for any actions performed using their unique login identity within the system.

Oct/Nov 2015

71. Which of the following should NOT be used when constructing a password, according to the guidelines?

(A) A complex mix of numerals, special characters, and both capital and lowercase letters.

(B) A known word that has been converted using numerals and special characters.

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statements is high. Conversely, it highlights that in a computerised system, the cost of preparing specialised management reports is negligible, allowing for easy generation of many customised reports.

Oct/Nov 2024

89. Regarding the disadvantages of computerised accounting, which of the following statements are correct?

1. It requires special programmes that can be costly.
2. It is prone to data loss, necessitating regular back-ups.
3. It eliminates the need for technically qualified staff.

(A) 1 and 2 only
(B) 2 and 3 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(A) 1 and 2 only
The text lists the requirement of special programmes and professionals (which can be costly) and the need for regular back-ups to guard against data loss as key disadvantages. However, it states that computerised accounting requires qualified staff for operations, which is also a disadvantage due to increased initial costs, directly contradicting statement 3.

May/June 2010

90. Evaluate the following statements about core banking solutions.

1. They enable real time on-line banking.
2. They support functions like lending, remittances, and clearing of cheques.
3. They operate on a decentralised model where each branch is independent.
4. They help banks provide 24x7 non-stop services.

Which combination of statements is correct?
(A) 1, 2, and 3 only
(B) 1, 2, and 4 only
(C) 2, 3, and 4 only
(D) 1, 3, and 4 only

Ans :

(B) 1, 2, and 4 only
The text confirms that core banking solutions facilitate real-time online banking (1), computerise various functions like lending and remittances (2), and enable 24x7 services (4). Statement (3) is incorrect because the text emphasizes that modern banking has moved away from a decentralised model to a centralised infrastructure, which is a core principle of CBS.

Oct/Nov 2016

91. Which of the following statements about computerised accounting is incorrect?
(A) The trail of transactions is easier to establish compared to a manual system.
(B) It has become more economical than employing a large number of people.
(C) A single entry can automatically update subsidiary books, ledgers, and financial statements.
(D) The risk of data manipulation is a real concern for users of financial statements.

Ans :

(A) The trail of transactions is easier to establish compared to a manual system.
The text explicitly states that establishing an acceptable audit trail, or the trail of events, "is more difficult" in computerised systems because data storage and manipulations are done inside the computer and are not physically visible. The other three statements are all presented as correct facts about computerised accounting within the chapter.

May/June 2025

92. Which statement accurately describes the role of computerisation in bank lending?
(A) Computerisation is only used for monitoring disbursements but not for charging interest.
(B) The entire lending process, including interest charging and monitoring, can be computerised.
(C) The lending function remains an entirely manual process in most modern banks.
(D) Computerisation in lending is limited to generating the initial loan application form.

Ans :

(B) The entire lending process, including interest charging and monitoring, can be computerised.
The text states that the lending function, much like the deposit function, is computerised in most banks. It specifies that work related to "charging of interest, monitoring of disbursements, inspection of the borrowing units and repayment schedule can be computerised and carried out

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Ans :

(A) After successfully logging in without any issues.
The text lists specific circumstances that mandate a password change: at least once every thirty days, when enforced by the system, if it has been shared, or if a compromise is suspected. Simply logging in successfully is a normal operation and does not trigger a requirement to change the password, unless one of the other conditions is also met.

May/June 2006

76. What is the 'Internet' defined as in the chapter?
(A) A single, large supercomputer owned and operated by a government agency.
(B) The inter-connection between several computers of different types belonging to various networks.
(C) A specific software application used for sending and receiving electronic mail.
(D) A proprietary series of servers interconnected through a single type of hypertext.

Ans :

(B) The inter-connection between several computers of different types belonging to various networks.
The text provides a precise definition of the Internet. It is described as "the inter-connection between several computers of different types belonging to various networks all over the globe." It is characterized as a "network of networks," highlighting its vast and heterogeneous nature, which connects millions of computers worldwide.

Oct/Nov 2017

77. What is the 'World Wide Web' (WWW)?
(A) A global network of physical computer hardware and network cables.
(B) A specific type of software for browsing websites, such as Chrome or Firefox.
(C) A series of servers that are interconnected through hypertext.
(D) The collection of physical cables and satellites that make up the internet.

Ans :

(C) A series of servers that are interconnected through hypertext.
The World Wide Web (WWW) is defined as an application that runs on the Internet. The text specifies that the "WWW is a series of servers that are interconnected through hypertext." This system allows users to navigate between documents and resources located on different servers using hyperlinks, creating a web of information.

May/June 2008

78. In the context of the World Wide Web, what is a 'hyperlink'?
(A) Highlighted text that, when selected, displays more information or navigates to another document.
(B) A type of browsing software used to navigate the web, such as Safari or Microsoft Edge.
(C) The primary index page or main landing page of an organization's website.
(D) The commercial act of buying and selling various products and services on the web.

Ans :

(A) Highlighted text that, when selected, displays more information or navigates to another document.
The text explains that hypertext is a method of presenting information where certain text is highlighted. It then defines these highlighted items as "hyperlinks". These links "allow the users to navigate from one document to another that may be located on different servers," forming the fundamental navigation mechanism of the World Wide Web.

Oct/Nov 2013

79. What is the term for the software, such as Internet Explorer, Chrome, or Mozilla Firefox, that helps users to navigate the WWW?
(A) Home Page
(B) Hypertext
(C) Browser
(D) E-commerce

Ans :

(C) Browser
The text states that a user can use "browsing software such as Internet Explorer, Chrome, Mozilla Firefox, Microsoft Edge, Safari etc. to navigate the web." It then provides a concise definition: "A browser is a software that helps the users to navigate the WWW," clearly identifying the function of these applications.

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synchronization enables—a seamless cross-channel experience without redundant data entry.

Oct/Nov 2025

97. Based on the following source text, which statement is NOT supported?
"A neo-bank is a bank that operates without a physical branch network, that is, the banking business is conducted entirely online... Some of the advantages of neo-banking include a simple account opening procedure, lower costs, and a simple and user-friendly interface."
(A) Neo-banks do not have physical branches.
(B) Neo-banks offer a simple account opening process.
(C) Neo-banks are guaranteed to be more profitable than traditional banks.
(D) Neo-banks typically have lower operational costs.

Ans :

(C) Neo-banks are guaranteed to be more profitable than traditional banks.
The source text clearly states that neo-banks operate without physical branches, have a simple account opening process, and offer lower costs. However, it makes no claim or guarantee about their profitability compared to traditional banks. While lower costs might contribute to profitability, the text does not make this assertion.

May/June 2023

98. A bank is planning to merge with another smaller bank. Which specific benefit of a modern core banking solution would be most critical to facilitate a smooth technological integration of the two entities?
(A) Support for multi-bank and single-bank operations.
(B) Automation of complex fee and interest rate calculations.
(C) Providing a fast-track Product Build component.
(D) Optimising transaction throughput.

Ans :

(A) Support for multi-bank and single-bank operations.
The text explicitly states that the ability to "Provide full multi-bank and single-bank operations... [is] to support mergers and acquisitions and other branding strategies." This feature is designed to handle the complexities of running multiple bank brands or integrating a new bank's operations onto a single platform, making it crucial for a merger scenario.

Oct/Nov 2014

99. A bank manager needs a report showing the profitability of a specific loan product for the last quarter, broken down by geographical area. Which function of computerised accounting software would directly address this need?
(A) The function for maintaining statutory books of account as required by law.
(B) The module for converting foreign currency transactions into the base currency.
(C) The capability to report profit earned on a product-wise and area-wise basis.
(D) The process for performing the valuation of closing stock of raw materials.

Ans :

(C) The capability to report profit earned on a product-wise and area-wise basis.
This scenario requires specific, granular profitability analysis. The text lists as a function that software is "capable of giving profit earned by the entity product-wise, area-wise, etc., and thus, help the management in planning." This directly matches the manager's requirement for a product-wise and area-wise profitability report for strategic planning.

May/June 2012

100. A user has left their core banking terminal unattended in the middle of a cash deposit transaction. Which security practice has been violated?
(A) The specific security practice of not leaving a terminal mid-transaction.
(B) The general company rule against sharing user passwords with any colleagues.
(C) The established IT policy to change system passwords at least once every month.
(D) The network security guideline to disable all folder sharing over the local network.

Ans :

(A) The specific security practice of not leaving a terminal mid-transaction.
This case directly violates a specific protection measure mentioned for core banking users. The text advises that "care should be taken not to leave the terminals in the middle of a

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(A) To process external transactions like salary files received from corporate clients.
(B) To create new customer information files (CIF) when onboarding a new customer.
(C) For internal transaction record posting, such as standing orders.
(D) To process the majority of customer-facing financial transactions online.

Ans :

(C) For internal transaction record posting, such as standing orders.
The text describes 'Online Day Journal' as a mechanism for further online processing. Its specific use is "for internal transaction record posting." The examples provided to illustrate this function are standing orders and batch interest updating programs, which are internal processes managed by the system rather than direct customer-initiated financial transactions.

May/June 2009

110. In the technical architecture of core banking, how are the branch servers connected to the central server (Hub)?
(A) Through a dedicated line
(B) Through the public internet
(C) Through a wireless satellite link only
(D) They are not connected; they operate independently

Ans :

(A) Through a dedicated line
The text describes the connectivity within the core banking architecture. It states that the branch servers will be connected to the central server (Hub). It further specifies that "The branches and the 'Host' will be connected through a dedicated line," ensuring a secure, reliable, and high-performance connection between the central data center and the branches.

Oct/Nov 2011

111. From the list of information security aspects, which are covered by a core banking solution?
1. Physical security
2. E-mail security
3. Capacity Management
4. Change Management
5. Customer complaint resolution

(A) 1, 2, 3, and 4 only
(B) 1, 2, 3, 4, and 5
(C) 2, 3, and 4 only
(D) 1, 2, and 5 only

Ans :

(A) 1, 2, 3, and 4 only
The chapter provides a detailed list of information security aspects. This list includes Physical security, E-mail security, Capacity Management, and Change Management. However, customer complaint resolution is a customer service function and is not included in this specific list of information systems security controls, making statement 5 the exception.

May/June 2017

112. Based on the following source text, why does establishing an audit trail become more difficult in a computerised system?
"The first difference relates to the trail of transactions or events, i.e. the ability to trace every entry in the ledger to its components in journals and eventually to the source documents... In computerised systems, creating an acceptable audit trail... becomes more difficult..."
(A) Because all original paper-based source documents are no longer used or retained.
(B) Because its data storage and arithmetic manipulations are not physically visible.
(C) Because modern computers do not use the traditional concepts of journals or ledgers.
(D) Because the system requires too many different passwords for accessing various data points.

Ans :

(B) Because its data storage and arithmetic manipulations are not physically visible.
The source text explains the difficulty arises because "the data storage and arithmetic manipulation are done inside the computer and are not visible physically." Unlike a manual system where one can physically trace an entry through different books, the internal, non-visible processing in a computer makes this trail harder to follow and verify.

Oct/Nov 2015

113. Based on the following source text, which type of computer is suitable for computerised accounting and why?
"Analogue computers are mostly used in scientific and mechanical fields and they process data in a continuous form. Digital computers, on the other hand, accept data and convert them into useful

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The text describes the layers as follows: The Presentation layer is the user interface. The Delivery layer is the interface between the front-end and OS. The Application layer contains the business logic driven by triggers. The Database layer interfaces with the database. Therefore, P matches with 3, Q with 4, R with 1, and S with 2.

Oct/Nov 2022

105. Match the term related to computerised accounting (List-I) with its correct example or definition (List-II).

List-I

P. Data
Q. Record
R. Data File
S. System

List-II

1. A sales register of invoices
2. A payroll file of 1,000 employees
3. Price, sales tax, date of sale
4. Computer machine, software, and peripherals

(A) P-1, Q-3, R-2, S-4
(B) P-3, Q-1, R-2, S-4
(C) P-3, Q-2, R-1, S-4
(D) P-1, Q-2, R-3, S-4

Ans :

(B) P-3, Q-1, R-2, S-4
The chapter defines these terms with specific examples. 'Data' (P) are raw facts like price and date of sale (3). A 'Record' (Q) is a group of related data, like a sales register (1). A 'Data File' (R) is a compilation of records, like a payroll file (2). A 'System' (S) comprises the components that process data (4).

May/June 2018

106. Which of the following pairs of a computerised accounting feature and its description is incorrectly matched?

(A) Speed : Managing 1,000 sales invoices daily in a short time.
(B) Economy : Human labour has become cheaper than computers.
(C) Accuracy : Preparing a trial balance in seconds without calculation mistakes.
(D) Report Generation : Preparing an area-wise sales list in a few minutes.

Ans :

(B) Economy : Human labour has become cheaper than computers.
The description for Economy is incorrect. The text states that computerised accounting has become cheaper because human labour has become costlier due to inflation, not cheaper. The other pairs correctly match the feature with the example or description provided in the text for Speed, Accuracy, and the ability to generate various reports.

Oct/Nov 2007

107. Which pair correctly matches the banking technology with its primary function?

(A) RTGS : Automation of standing instructions.
(B) CTS : Providing 24/7 cash withdrawal facility.
(C) NEFT : Remittance of money to other centres.
(D) ATM : Faster clearing of cheques by transmitting images.

Ans :

(C) NEFT : Remittance of money to other centres.
The text lists NEFT, along with RTGS and IMPS, as a technology used for remittances, which is arranging to remit money to other centres. CTS is for cheque clearing, not cash withdrawal. ATMs provide 24/7 cash withdrawal. Standing instructions are automated by the core banking system itself, not specifically by RTGS.

May/June 2014

108. Which of the following is NOT a benefit of online processing in a core banking system?

(A) It requires significant downtime for Day-end or batch processing.
(B) The entire database and all transactions are always available.
(C) It allows for a flexible system and eases change.
(D) It optimises transaction throughput.

Ans :

(A) It requires significant downtime for Day-end or batch processing.
The text lists the benefits of online processing, and one of the key benefits mentioned is "No downtime for Day-end or batch processing." This is because transactions are processed in real-time, eliminating the need to halt the system for end-of-day procedures. The other options are all listed as direct benefits of online processing.

Oct/Nov 2019

109. What is the function of an 'Online Day Journal' in a core banking system?

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(C) A virus can destroy all data on a computer, including any back-up copies.

The text describes a computer virus as a mischievous software that damages data. It highlights the severity of this risk by stating that a virus "may destroy the entire data in a computer and those kept in a back-up." This potential to corrupt not just live data but also recovery copies makes it a particularly serious threat.

May/June 2022

126. What is the primary reason banks moved from a decentralised to a centralised infrastructure?

(A) To increase the operational autonomy and independence of individual branches.
(B) To address the need for an instantaneously updated database for multi-channel services.
(C) To reduce the overall need for trained manpower and expensive hardware.
(D) To comply with a new regulatory mandate that required decentralisation of data.

Ans :

(B) To address the need for an instantaneously updated database for multi-channel services.

The text explains that the decentralised model was acceptable "till multi-channel came into the picture." With the advent of multiple channels, "came the need for a centralised database" that had to be "updated instantaneously irrespective of the branch or channel the customer used," driving the shift to a centralised architecture.

Oct/Nov 2018

127. Which of the following is a key benefit of core banking that helps in reducing operational expenses?

(A) Supporting complex multi-currency and multi-language operations.
(B) Extending system functionality through the use of custom user-exits.
(C) Supporting full multi-bank and single-bank operations for mergers.
(D) Providing the opportunity to rationalise processing infrastructure.

Ans :

(D) Providing the opportunity to rationalise processing infrastructure.

The text lists as a benefit that core banking "Provides the opportunity to rationalise processing infrastructure with resulting cost reductions and increased operational resilience." By centralizing and streamlining the IT infrastructure, banks can eliminate redundant systems and hardware at the branch level, leading to significant cost savings in maintenance and management.

May/June 2021

128. In the maker-checker functionality described for TCS BaNCS, what is generated and displayed in the system once a teller initiates a transaction that requires authorization?

(A) A queue number
(B) An error message
(C) A transaction receipt
(D) A confirmation code

Ans :

(A) A queue number

The text details the process: "Once the transaction is initiated by the teller a queue number will be generated and displayed in the system." This queue number acts as a unique identifier for the pending transaction, which the authorizing supervisor then uses to locate and approve the specific item in the queue management module.

Oct/Nov 2005

129. What security measure should a user adopt to prevent unauthorized access if they are leaving their desktop unattended at any time?

(A) Enable the screen saver with password protection.
(B) Disable the sharing of all folders over the network.
(C) Log out of all applications.
(D) Change their password before leaving the desk.

Ans :

(C) Log out of all applications.

The text provides specific guidance for this scenario. Under protection measures, it states the user should "(a) Log out of all applications, if leaving the desktop unattended at any time." This is a more secure measure than just a screen saver for longer or indefinite periods of absence, as it completely terminates the user's sessions.

May/June 2013

130. What is a key advantage of neo-banking that appeals to its target audience?

(A) A simple account opening procedure and user-friendly interface.
(B) The ability to interact with a human teller in

NODIA

results by carrying out arithmetic operations..."

(A) Analogue, because accounting data is typically presented in a continuous form.

(B) Digital, because it performs arithmetic operations on discrete data.

(C) Hybrid, because accounting requires both scientific and arithmetic processing.

(D) Analogue, because it is generally faster than a digital computer for financial tasks.

Ans :

(B) Digital, because it performs arithmetic operations on discrete data.

The source text clearly distinguishes between the two. It states that digital computers "accept data and convert them into useful results by carrying out arithmetic operations," which is the fundamental nature of accounting transactions (e.g., adding debits, subtracting credits). Analogue computers process continuous data, which is not typical of financial transactions.

May/June 2020

114. Based on the following source text, which major challenge for a multi-branch entity does this function primarily help overcome?

"In case of an entity having branches all over India and abroad, the software maintains accounts of all the branches and the head office. The software also prepares a consolidated trial balance and financial statement of the entity as a whole."

(A) The complexity and time required for the account consolidation process.

(B) The difficulty of processing transactions that are denominated in foreign currency.

(C) The challenge of accurately valuing the company's year-end inventory holdings.

(D) The effort involved in generating detailed area-wise sales performance reports.

Ans :

(A) The complexity and time required for the account consolidation process.

The source describes the software's ability to maintain accounts for all branches and the head office and, crucially, to prepare a "consolidated trial balance and financial statement." This directly addresses the significant accounting challenge of combining the financial data from numerous, often geographically dispersed, branches into a single, unified report for the entire entity.

Oct/Nov 2021

115. Based on the following source text, what was a direct consequence of the described decentralised model?

"In the early days of banking technology, the network/backend infrastructure used to be decentralised. This meant that each branch had its own server(s), banking applications, database(s), and other such assorted hardware and software."

(A) Each branch operated as a separate technological silo.

(B) Significantly lower capital expenditure and resource requirements.

(C) A single, unified view of the customer was available across the bank.

(D) Application updates and troubleshooting were simplified and centralized.

Ans :

(A) Each branch operated as a separate technological silo.

The source states that in the decentralised model, each branch had its "own server(s), banking applications, database(s)." This structure inherently means that each branch was a self-contained unit or a technological silo. This led to problems like high costs, lack of coordination, and no single customer view, which were later solved by centralisation.

May/June 2024

116. A new account's specific interest calculation rules, fee structure, and features, and make it available across all branches immediately. This demonstrates which benefit of core banking?

(A) Rationalising processing infrastructure.

(B) Delivering speed to market in product development.

(C) Supporting multi-currency operations.

(D) Providing data for compliance and risk management.

Ans :

(B) Delivering speed to market in product development.

This scenario is a practical example of "speed to market." The text explains that core banking allows for rapid product development via the Product Build component. The ability to quickly

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define and deploy a new product like the high-yield savings account, making it instantly available, is a direct manifestation of this key strategic benefit.

Oct/Nov 2008

117. A customer starts a loan application on their mobile banking app but needs to submit physical documents at a branch. The branch officer is able to retrieve the partially filled application and continue the process from where the customer left off. This seamless experience is a hallmark of which banking concept?
(A) Neo-banking
(B) Omni-channel banking
(C) Decentralised banking
(D) Manual banking

Ans :

(B) Omni-channel banking
The text describes omni-channel banking as providing a consistent experience and synchronizing data across all channels. The example of starting a process on one channel (mobile app) and finishing it on another (physical branch) without re-entering information is a classic illustration of the omni-channel concept in action, as described in the chapter.

May/June 2006

118. A bank employee receives an email with an urgent request to open an attachment to view a new security policy. The attachment, however, is a malicious file. This scenario represents a threat related to which aspect of information security?
(A) E-mail security
(B) Physical security
(C) Password management
(D) Desktop security

Ans :

(A) E-mail security
This is a typical example of a phishing or malware attack delivered via email. The chapter lists "E-mail security" as a key area covered under the broader umbrella of information security. Protecting against malicious attachments and deceptive emails falls directly under this category, which aims to secure this common communication channel from threats.

Oct/Nov 2017

119. During a system audit, it is found that an accountant is using the password "1secret". This violates the password construction guideline that prohibits what?
(A) Using personal information such as a date of birth.
(B) Using a password that is shorter than eight characters.
(C) Using common dictionary words preceded or followed by a digit.
(D) Using keyboard patterns such as 'qwerty' or 'asdfgh'.

Ans :

(C) Using common dictionary words preceded or followed by a digit.
The password construction guidelines explicitly state that "Any of the above words [including common dictionary words] preceded or followed by a digit (e.g. secret1, 1secret) should not be used." The password "1secret" is a direct example of this poor practice, as it uses a common word with a simple prefix, making it weak and easy to guess.

May/June 2008

120. A bank decides to offer services via WhatsApp for balance inquiries and mini-statements. This initiative to provide services on a social media platform is an example of which banking strategy?
(A) Omni-channel banking
(B) Neo-banking
(C) Centralised banking
(D) Automated banking (ATM)

Ans :

(A) Omni-channel banking
The text defines omni-channel banking as providing services across all channels, and it explicitly gives examples of "social media platforms such as WhatsApp, Facebook or Instagram." Extending banking services to a platform like WhatsApp is a clear implementation of an omni-channel strategy, meeting customers on the platforms they already use.

Oct/Nov 2013

121. The ability of a computerised system to perform millions of operations without committing an error, unlike a human being, is referred to as which advantage?

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(A) High Speed Operation
(B) Availability of Various Reports
(C) Low Cost of Operation
(D) Error-free Accounting

Ans :

(D) Error-free Accounting
The text highlights "Error-free Accounting" as a distinct advantage. It explains that a computer can perform millions of operations without committing any error, which is a feat impossible for a human being. This reliability in computation ensures the accuracy of financial records once the initial data has been entered correctly into the system.

May/June 2015

122. In a multi-user computerised accounting system like a LAN, what is the typical role of each user?
(A) Each user is independently responsible for the entire accounting cycle from start to finish.
(B) Each user handles a specific segment of transactions, such as sales or purchases.
(C) All users perform the exact same task simultaneously to ensure data entry accuracy.
(D) Users are only permitted to view and analyze data but are not allowed to enter it.

Ans :

(B) Each user handles a specific segment of transactions, such as sales or purchases.
The text describes the functioning of a multi-user system by stating that "each user handles a particular segment of the transactions only, say, either sales, purchase, cash, bank, etc." This division of labor allows for parallel processing of different transaction types, contributing to faster overall data feeding and processing in the system.

Oct/Nov 2020

123. The text states that "Modern accounts are more like computer-keeping rather than bookkeeping." What does this phrase imply?
(A) That fundamental accounting principles are no longer relevant in a computerised environment.
(B) The focus has shifted from manual record-keeping to managing accounts on a computer.
(C) Computers have completely and entirely replaced the professional role of accountants.
(D) The process of bookkeeping has become significantly more complex with the use of computers.

Ans :

(B) The focus has shifted from manual record-keeping to managing accounts on a computer.
This phrase highlights the fundamental shift in the accounting process. It suggests that the traditional manual task of "bookkeeping" (writing in books) has been replaced by the task of "computer-keeping" (managing data within a computer system). It emphasizes the change in method from manual entry to system-based management of financial records.

May/June 2011

124. What is the primary role of a 'programme' in a computer system?
(A) A set of instructions for solving a specific problem.
(B) The primary physical component that processes data.
(C) The raw information or facts fed into the computer.
(D) The final output or result generated by the computer.

Ans :

(A) A set of instructions for solving a specific problem.
The text defines a computer as a device that processes information according to a set of instructions. It further clarifies that the computer stores "sets of instructions for solving problems (i.e. set of software called programme)." This indicates that a programme is a specific set of software instructions designed to accomplish a particular task.

Oct/Nov 2023

125. Why is the risk of data loss from computer viruses a significant disadvantage of computerised accounting?
(A) A virus can only damage the computer's physical hardware, not the stored data.
(B) Modern anti-virus software is not effective against any known computer viruses.
(C) A virus can destroy all data on a computer, including any back-up copies.
(D) Viruses primarily affect manual accounting systems, not computerised systems.

Ans :

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transaction." Doing so creates a significant risk, as an unauthorized person could potentially alter or misuse the open, active transaction session.

Oct/Nov 2006

101. An employee suspects their password might have been compromised after noticing it written on a sticky note that was briefly misplaced. What is the immediate required action according to the password protection policy?

(A) Wait for the system-enforced mandatory 30-day password change cycle to complete.
(B) Report the potential compromise to the IT department and wait for their official instructions.
(C) Continue using the current password but resolve to be more careful about its security in the future.
(D) Change the password as soon as possible after suspecting it has been compromised.

Ans :

(D) Change the password as soon as possible after suspecting it has been compromised.
The policy outlines several triggers for a password change. One of these is: "As soon as possible, after a password has been compromised or after you suspect that a password has been compromised." The employee's suspicion is sufficient grounds to trigger this rule, requiring an immediate password change to mitigate the risk.

May/June 2019

102. Given the following statements: **Assertion (A) :** In a decentralised banking infrastructure, there were problems with updating applications and troubleshooting.
Reason (R) : The decentralised model lacked a single central control point and coordination between branches.

(A) Both A and R are true, and R is the correct explanation of A.
(B) Both A and R are true, but R is not the correct explanation of A.
(C) A is true, but R is false.
(D) A is false, but R is true.

Ans :

(A) Both A and R are true, and R is the correct explanation of A.
The text states that in the decentralised model, there were problems with updating applications and troubleshooting. It then explains that this was because "there is no coordination or one central control point." The lack of central control directly caused the difficulties in management and updates, making R the correct explanation for A.

Oct/Nov 2010

103. Given the following statements: **Assertion (A) :** Customer Relationship Management (CRM) is less important in modern banking because products can be copied very fast.
Reason (R) : In a hypercompetitive environment, customer service levels are what matter most for retaining customers.

(A) A is false, but R is true.
(B) Both A and R are true, and R is the correct explanation of A.
(C) Both A and R are true, but R is not the correct explanation of A.
(D) A is true, but R is false.

Ans :

(A) A is false, but R is true.
Assertion (A) is false; the text argues that because products are easily copied, CRM and service levels become more important, not less. Reason (R) is true, as the text states, "It is the customer service levels which matter." The reason explains why CRM is important, directly contradicting the false assertion.

May/June 2005

104. Match the system layer in core banking architecture (List-I) with its function (List-II).

List-I
P. Presentation layer
Q. Delivery layer
R. Application layer
S. Database layer

List-II
1. Driven by system triggers and parameters
2. Interfaces to database using call levels
3. The user-facing layer
4. Interface between front-end and operating system

(A) P-3, Q-4, R-1, S-2
(B) P-1, Q-2, R-3, S-4
(C) P-3, Q-1, R-4, S-2
(D) P-4, Q-3, R-2, S-1

Ans :

(A) P-3, Q-4, R-1, S-2

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a physical branch.

(C) Access to complex trade finance and corporate treasury services.

(D) The availability of services only during traditional 9-to-5 banking hours.

Ans :

(A) A simple account opening procedure and user-friendly interface.

The text highlights that the appeal of neo-banks to tech-savvy users comes from their advantages. Among these are "a simple account opening procedure, lower costs, and a simple and user-friendly interface." This focus on convenience, simplicity, and a positive digital user experience is a core part of their value proposition.

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CHAPTER 19

Financial Management – An Overview

May/June 2016

1. According to the introductory section, what is the primary role of funds in a business organisation?
(A) To exclusively pay promoter salaries and recurring dividends
(B) To create fixed assets and provide for working capital
(C) To primarily serve as a reserve for unforeseen legal liabilities
(D) To be used only for short-term operational or administrative expenses

Ans :

(B) To create fixed assets and provide for working capital
The introduction states that funds are crucial for business activities. They are needed for creating fixed assets, which form the productive base of the business, and for working capital, which is essential for day-to-day operations. Both are fundamental for a business to function and grow, moving beyond the initial capital provided by owners.

Oct/Nov 2009

2. What does the term 'Financial Management' essentially mean?
(A) Applying management principles to the financial resources and activities of an organisation
(B) The process of only recording financial transactions and preparing summary statements
(C) The function of exclusively raising funds through borrowings and issuing new equity
(D) The management of only the revenue-generating and sales aspects of a business

Ans :

(A) Applying management principles to the financial resources and activities of an organisation
Financial Management is broadly defined as the application of management principles like planning, organizing, conducting, and controlling to the financial activities and resources of an organisation. This encompasses the management of assets, liabilities, and revenues to achieve the firm's objectives, making it a comprehensive function beyond just fundraising or accounting.

May/June 2023

3. Which of the following is NOT listed as a form of business organisation?
(A) Limited Liability Partnership (LLP)
(B) Hindu Undivided Family (HUF)
(C) Non-Governmental Organisation (NGO)
(D) Association of Persons (AOP)

Ans :

(C) Non-Governmental Organisation (NGO)
The text explicitly lists several forms of business organisations: Sole Proprietary, Partnership Firm, Limited Liability Partnership (LLP), Hindu Undivided Family (HUF), Association of Persons (AOP) or Body of Individuals (BOI), Company, and Co-operative society. A Non-Governmental Organisation (NGO) is not mentioned in this specific list of business forms.

Oct/Nov 2018

4. Why is the initial choice of a business organisation form considered a very careful decision for promoters?
(A) Because it exclusively determines the number of employees a business can hire
(B) Because it is legally impossible to change the established form once operations begin
(C) Because the initial choice dictates the permanent marketing strategy of the firm
(D) Because changing the form later may attract significant tax liability

Ans :

(D) Because changing the form later may attract significant tax liability
The text highlights that the choice of business form must be exercised very carefully. The primary reason cited is that altering the organisational structure after the business has

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commenced operations can lead to significant tax implications. This makes the initial decision a critical one with long-term financial consequences for the business and its owners.

May/June 2007

5. In a Sole Proprietary firm, how is the profit of the business taxed?

(A) It is taxed separately from the owner at a corporate tax rate
(B) It is generally exempt from all forms of direct income taxation
(C) It is taxed as the personal income of the proprietor
(D) It is taxed at a special flat rate applicable only to proprietorships

Ans :

(C) It is taxed as the personal income of the proprietor
A key feature of a sole proprietorship is the absence of legal distinction between the owner and the firm. Consequently, the profits generated by the business are not taxed separately. Instead, they are considered the personal income of the sole proprietor and are taxed accordingly under the individual's income tax slab.

Oct/Nov 2025

6. What is a major limitation faced by a Sole Proprietary form of organisation?

(A) Excessive government regulation and complex compliance oversight
(B) Limitation of capital due to the owner's limited personal resources
(C) The significant complexity involved in its legal formation process
(D) The requirement to file audited financial statements with a regulator

Ans :

(B) Limitation of capital due to the owner's limited personal resources
While a sole proprietorship is the simplest form of business with minimum regulations, its primary disadvantage is the limitation of capital. The ability to raise funds is restricted to the personal resources and borrowing capacity of the single owner. This can significantly constrain the growth and scalability of the business operations.

May/June 2012

7. According to Section 4 of the Indian Partnership Act, 1932, what is the fundamental basis of a partnership?

(A) A government mandate requiring multiple owners for certain businesses
(B) A shared family relationship or bloodline among all the members
(C) The mandatory registration of the firm with a government authority
(D) An agreement between persons to share the profits of a business

Ans :

(D) An agreement between persons to share the profits of a business
The definition of partnership under the Indian Partnership Act, 1932, is centered on the concept of an agreement. It is a "relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all." This contractual agreement is the cornerstone of the partnership structure.

Oct/Nov 2014

8. What is the maximum number of partners a partnership firm can have as per the Companies Act 2013 and associated rules?

(A) 50
(B) 20
(C) 100
(D) 200

Ans :

(A) 50
Although the Indian Partnership Act, 1932, does not specify a maximum number of partners, the Companies Act, 2013, and the Companies (Miscellaneous) Rules, 2014, impose a limit. According to these provisions, a partnership firm can have a maximum of 50 partners. This rule prevents large, unregistered associations from operating as partnerships.

May/June 2019

9. Which statement correctly distinguishes a Limited Liability Partnership (LLP) from a traditional partnership firm?

(A) An LLP imposes unlimited personal liability for all its partners, unlike a partnership
(B) Registration is mandatory for a partnership but remains optional for an LLP
(C) An LLP is a separate legal entity, whereas a

NODIA

Ans :

(D) The return given up from the next best alternative investment

The principle of opportunity cost means that when you deploy money in one investment, you forgo the opportunity to invest it elsewhere. The opportunity cost is the potential return you could have earned from the best alternative investment that was not chosen. This concept is crucial for evaluating both new and existing investments.

Oct/Nov 2015

28. What is the general relationship between risk and return in finance?

(A) Higher risk is generally associated with higher potential rates of return

(B) Higher risk is generally associated with lower potential rates of return

(C) Lower risk is generally associated with higher potential rates of return

(D) There is no consistent or predictable relationship between risk and return

Ans :

(A) Higher risk is generally associated with higher potential rates of return

The fundamental principle of Risk and Return states that investments involve both a reward (profit) and a risk (loss). The normal relationship is that to achieve a higher potential rate of return, an investor must be willing to accept a higher level of risk. Conversely, lower-risk investments typically offer lower potential returns.

May/June 2013

29. The principle of 'Liquidity and Return' suggests a trade-off. What does this imply for a highly liquid investment?

(A) It typically offers the highest possible rate of return

(B) It is usually very difficult to convert into cash quickly

(C) It often does not provide the desired or a high rate of return

(D) It is only suitable for long-term, non-retrievable investment goals

Ans :

(C) It often does not provide the desired or a high rate of return

The principle highlights a trade-off between liquidity and return. Liquidity refers to how easily an investment can be sold and converted into cash. While high liquidity is desirable, the text states that a highly liquid investment often does not yield the desired or a high rate of return. Investors must balance their need for liquidity against their return objectives.

Oct/Nov 2021

30. What does the principle of 'Diversification' advise an investor to do?

(A) Spread investments across many different assets to reduce overall risk

(B) Invest all available money in a single, high-performing asset

(C) Only invest in highly liquid assets like cash and bank deposits

(D) Avoid all investments that carry any discernible level of risk

Ans :

(A) Spread investments across many different assets to reduce overall risk

The principle of diversification advises against concentrating all funds in one or two investments. Instead, it suggests spreading the money across multiple investments to mitigate risk. This follows the idiom, "never put all your eggs in one basket," as the poor performance of one asset can be offset by the better performance of others.

May/June 2024

31. The principle of 'Reducing asset-liability mismatch' or 'Hedging' suggests a specific funding strategy. What is it?

(A) Short-term fund requirements should be primarily met from long-term sources

(B) Long-term fund requirements should be primarily met from short-term sources

(C) All fund requirements, regardless of term, should be met only from equity

(D) Long-term fund requirements should be met from long-term sources

Ans :

(D) Long-term fund requirements should be met from long-term sources

This principle, also known as the matching principle or hedging, implies that the maturity of funding sources should match the maturity of the assets being financed. As far as feasible, long-term fund requirements (e.g., for fixed assets) should be met from long-term sources (e.g.,

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emphasizes the legal process of incorporation as the defining characteristic of a company.

Oct/Nov 2022

14. What feature distinguishes a co-operative society from other forms of business organisations?
(A) Its primary aim is maximizing profit for its external shareholders
(B) It is managed by a single owner known as the proprietor
(C) It does not possess a separate legal identity from its members
(D) Its main objectives are mutual assistance and service for its members

Ans :

(D) Its main objectives are mutual assistance and service for its members
The defining characteristic of a co-operative society is its focus on promoting the common goals of its members through mutual assistance and service. This contrasts with other business forms, such as companies, where the primary objective is typically profit maximization for the owners or shareholders.

May/June 2018

15. Which of the following is NOT considered one of the primary financial decisions in a firm?
(A) Determining the marketing and advertising budget for a new product
(B) Estimating the total short-term and long-term capital requirements
(C) Deciding the optimal capital structure or composition of funds
(D) Choosing the specific long-term and short-term sources of funds

Ans :

(A) Determining the marketing and advertising budget for a new product
The text lists several key financial decisions, including estimating capital needs, deciding on capital structure (debt-equity mix), choosing sources of funds, and managing long-term and short-term funds. While marketing budgets have financial implications, determining the marketing strategy itself is typically a marketing function, not a primary financial decision.

Oct/Nov 2016

16. In the context of financial decisions, what is the significance of deciding the capital structure?
(A) It determines the firm's physical location and corporate headquarters
(B) It plays a crucial role in the profitability and sustainability of operations
(C) It primarily affects the hiring and compensation policies for employees
(D) It is a decision that is only relevant for government and non-profit organisations

Ans :

(B) It plays a crucial role in the profitability and sustainability of operations
Deciding the capital structure, which is the mix of debt and equity, is a crucial financial decision. A high proportion of debt can endanger profitability and viability due to servicing costs, while low debt might lead to under-utilization of the firm's profit-earning potential. Therefore, this mix directly impacts profitability and long-term sustainability.

May/June 2014

17. What is a key objective when deciding on the sources of funds for a firm?
(A) To exclusively raise all required funds from international capital markets
(B) To select a mix of sources that optimizes the firm's Weighted Average Cost of Capital (WACC)
(C) To maximize the amount of debt financing regardless of the associated cost or risk
(D) To rely solely on public deposits and debentures for all financing needs

Ans :

(B) To select a mix of sources that optimizes the firm's Weighted Average Cost of Capital (WACC)
When selecting from various sources of finance like equity, preference shares, debentures, or loans, each with its own merits and demerits, a central goal is to optimize the overall cost. This is achieved by minimizing the Weighted Average Cost of Capital (WACC), which represents the blended cost of all capital sources.

Oct/Nov 2007

18. What does the financial decision regarding the 'Use of long term funds' primarily involve?
(A) Capital budgeting, which is the selection of long-term investment proposals
(B) The day-to-day management of operational cash flows and liquidity
(C) Deciding the annual dividend payout

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(B) Potential return rises when higher risk is taken, and vice versa

The risk-return trade-off is a core principle in finance. It states that there is a direct relationship between the amount of risk taken and the potential return. To have a chance at earning higher returns, one must accept a higher level of risk. Conversely, if one chooses to take lower risk, they must be content with lower potential returns.

May/June 2015

37. How is 'Risk' defined in the context of the risk-return trade-off?

(A) The certainty that an investment will generate a specific, guaranteed profit
(B) The process of optimizing the firm's Weighted Average Cost of Capital (WACC)
(C) The possibility that the actual return will be less than the forecast return
(D) The strategy of relying solely on public deposits and debentures for funding

Ans :

(C) The possibility that the actual return will be less than the forecast return

Risk in an investment context is defined as the possibility or probability that the actual return realized from an investment will be different from, specifically less than, the expected or forecast return. It represents the uncertainty associated with the investment's outcome, and this element of uncertainty is inherent in every investment.

Oct/Nov 2012

38. What is the formula provided for the 'Required Rate of Return'?

(A) Required Rate of Return = Risk Premium - Risk-free Return
(B) Required Rate of Return = Risk-free Return + Risk Premium
(C) Required Rate of Return = Risk-free Return / Risk Premium
(D) Required Rate of Return = Risk-free Return × Risk Premium

Ans :

(B) Required Rate of Return = Risk-free Return + Risk Premium

The text expresses the relationship between the required rate of return and risk with the formula: Required Rate of Return = Risk-free Return + Risk Premium. This shows that the return an investor demands is the sum of the return on a risk-free asset (like a government bond) and an additional premium to compensate for the specific risk of the investment.

May/June 2011

39. Which type of investment is generally considered to be 'risk-free'?

(A) Investment in high-yield junk bonds
(B) Investment in the common stock market
(C) Investment in Government bonds
(D) Investment in a new technology startup company

Ans :

(C) Investment in Government bonds

Investment in government bonds is considered to be risk-free or having almost nil risk of default. The interest rate is known, and the government's ability to meet its debt obligations is considered certain. This risk-free rate serves as a benchmark for determining the required return on all other, riskier investments.

Oct/Nov 2020

40. Under what circumstances does an 'Agency Problem' typically arise in financial management?

(A) When there is a separation of ownership and management
(B) When there is a merger of two companies of equal size
(C) When a company's annual profits significantly exceed its forecasts
(D) When a company successfully issues new bonds to the public

Ans :

(A) When there is a separation of ownership and management

An agency problem is a conflict of interest that typically arises when there is a separation between the ownership of a business (the principals, e.g., shareholders) and the management of that business (the agents, e.g., managers). The conflict occurs when managers (agents) may act in their own self-interest rather than the best interests of the owners.

May/June 2022

41. In a large company, who are considered the 'principals' and who are the 'agents' in the primary agency relationship?

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May/June 2010

23. Why might a company choose to buy back its shares instead of paying a dividend?

(A) Because regular share buybacks are legally mandatory for all listed companies

(B) Because buybacks significantly increase the number of outstanding shares

(C) Because cash dividends are typically taxable as income for the shareholders

(D) Because cash dividends are generally considered a tax-deductible business expense

Ans :

(C) Because cash dividends are typically taxable as income for the shareholders

The text states that firms sometimes decide to benefit shareholders through a buyback of shares instead of a cash dividend. A key reason for this choice is the tax implication; cash dividends are treated as income and are taxable in the hands of the shareholders, which can be less tax-efficient than a buyback.

Oct/Nov 2024

24. Which of the following is listed as a primary objective of financial management?

(A) To maximize the company's total sales volume regardless of cost

(B) To minimize all forms of financial and operational risk to zero

(C) To maintain the highest possible cash balance at all times

(D) To ensure an adequate and timely supply of funds at a reasonable cost

Ans :

(D) To ensure an adequate and timely supply of funds at a reasonable cost

One of the primary objectives of financial management summarized in the text is to ensure a sufficient and timely availability of both long-term and short-term funds for the organisation. Crucially, these funds must be procured at a reasonable cost to maintain the financial health and profitability of the firm.

May/June 2017

25. Which one of the following is NOT an objective of financial management?

(A) To handle all human resource and employee recruitment functions

(B) To ensure the optimum utilization of all procured funds

(C) To decide on an optimum capital structure for the firm

(D) To ensure statutory and regulatory compliance in financial matters

Ans :

(A) To handle all human resource and employee recruitment functions

The text lists several objectives of financial management, including optimum fund utilization, deciding on capital structure, making sound investment decisions, and ensuring compliance. Handling human resource functions like recruitment and employee management falls under the purview of the HR department, not financial management, although there are financial aspects to it.

Oct/Nov 2005

26. The principle of 'Time Value of Money' states that a rupee received today is more valuable than a rupee received in the future. What is the reason for this?

(A) Solely because of the persistent and eroding effects of inflation

(B) Because money received today has earning power through proper investment

(C) Only because of the inherent risk of not receiving the future rupee

(D) Because future money is always subject to significantly higher tax rates

Ans :

(B) Because money received today has earning power through proper investment

The text explains that the time value of money is not just due to inflation. A primary reason is that money received today has earning power; it can be invested to generate returns. This potential to earn interest or profit is why a person would be willing to pay interest to borrow money now.

May/June 2020

27. What does the 'Opportunity Cost of Money' principle imply?

(A) The need to exclusively raise funds from international markets

(B) The goal to optimize the firm's Weighted Average Cost of Capital (WACC)

(C) The strategy to maximize the amount of debt regardless of cost

(D) The return given up from the next best alternative investment

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percentage to all shareholders
(D) The process of filing statutory tax returns with government authorities

Ans :

(A) Capital budgeting, which is the selection of long-term investment proposals
The use of long-term funds is synonymous with the long-term investment decision, also known as Capital Budgeting. This crucial process involves choosing from various capital asset or investment proposals, such as acquiring new assets or replacing old ones, whose benefits are expected to accrue over a long period.

May/June 2025

19. Which of the following techniques is used for the appraisal of long-term investment decisions?
(A) Ratio Analysis
(B) Budgetary Control
(C) Internal Rate of Return (IRR)
(D) Standard Costing

Ans :

(C) Internal Rate of Return (IRR)
The text mentions that for appraising long-term investment decisions, various techniques are employed to assess the return on capital. It explicitly lists Internal Rate of Return (IRR), Net Present Value (NPV), and Pay Back Period as methods used for these investment decisions. Ratio analysis, budgetary control, and costing are for financial control.

Oct/Nov 2019

20. How is 'inorganic growth' of an organisation typically achieved?
(A) By acquiring the businesses of other firms through mergers and acquisitions
(B) By expanding the business through creating additional internal capacity
(C) By increasing marketing expenditure to gain a larger market share
(D) By implementing internal cost-control measures to improve profitability

Ans :

(A) By acquiring the businesses of other firms through mergers and acquisitions
The text distinguishes between organic and inorganic growth. Organic growth involves internal expansion by creating new capacity. In contrast, inorganic growth is achieved externally by acquiring other firms. This route, through mergers and acquisitions, offers benefits like saving time on capacity creation and potentially reducing competition.

May/June 2009

21. What is the major trade-off that needs to be managed in working capital management?
(A) The trade-off between long-term assets and short-term assets
(B) The trade-off between equity financing and debt financing
(C) The trade-off between domestic sales and international sales
(D) The trade-off between profitability and liquidity

Ans :

(D) The trade-off between profitability and liquidity
Working capital management involves managing current assets and liabilities. A major task within this function is balancing profitability and liquidity, which are inversely related. Maintaining high liquidity (e.g., holding excess cash) ensures smooth operations but can hurt profitability, as idle cash is an unproductive resource.

Oct/Nov 2011

22. What is the purpose of 'Financial Control' in financial management?
(A) To focus exclusively on the process of raising new capital
(B) To monitor activities, identify inefficiency, and take corrective action
(C) To prepare the company's final accounts solely for the annual audit
(D) To ensure the timely payment of salaries to all company employees

Ans :

(B) To monitor activities, identify inefficiency, and take corrective action
The function of financial management extends beyond just raising and using funds. Financial control involves the continuous monitoring of all financial activities. Its purpose is to spot any areas of inefficiency or deviations from the plan and to initiate timely corrective measures. Techniques like ratio analysis and budgetary control are used for this.

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equity, term loans), and short-term needs from short-term sources.

Oct/Nov 2008

32. What are the two aspects involved in the 'Cash Flow' principle of finance?

(A) Maximizing accounting profit while simultaneously minimizing all operational expenses
(B) Managing liquidity via cash flows and discounting them for their time value
(C) Acquiring long-term fixed assets and managing short-term current liabilities
(D) Issuing new equity shares to the public and repaying existing corporate debt

Ans :

(B) Managing liquidity via cash flows and discounting them for their time value
The cash flow principle has two key facets. First, it involves balancing cash inflows and outflows over a period to ensure the firm has adequate liquidity to meet its obligations. Second, it incorporates the time value of money principle by appropriately discounting future cash inflows to determine their present value for decision-making.

May/June 2006

33. According to the modern approach, which of the following is one of the four basic building blocks of the corporate finance function?

(A) Marketing
(B) Human Resources
(C) Decision Making
(D) Production

Ans :

(C) Decision Making
The modern approach to corporate finance is built on four basic blocks. These are listed as Planning, Decision making, Organising and Directing, and Controlling. Decision making in this context refers to making investment, financing, and profit distribution decisions after evaluating the viability of plans.

Oct/Nov 2017

34. In the context of the building blocks of modern finance, what does 'Controlling' involve?

(A) The initial one-time decision to approve or reject a project
(B) The physical execution and construction phase of a project
(C) The process of raising the necessary funds for an approved plan
(D) Keeping a continuous watch on activities to identify deviations from the plan

Ans :

(D) Keeping a continuous watch on activities to identify deviations from the plan
The controlling function does not end once a decision is made and implemented. It involves a continuous watch over the firm's activities to identify any deviations from the approved plan, such as cost or time overruns in a project. This allows for timely corrective actions to ensure the project's viability is not compromised.

May/June 2008

35. Besides the four basic blocks (Planning, Decision Making, etc.), an alternative classification of building blocks for modern financial management is mentioned. Which of the following is part of this alternative list?

(A) Transparency
(B) Profitability
(C) Market Share
(D) Employee Satisfaction

Ans :

(A) Transparency
The text presents another classification of building blocks for modern financial management. This list includes Consistency, Accountability, Transparency, Viability, Integrity, Management, and Accounting Standards. Transparency is explicitly mentioned as one of these fundamental building blocks, emphasizing openness in financial operations and reporting.

Oct/Nov 2013

36. What is the fundamental concept of the 'Risk-Return Trade-off'?

(A) Higher risk must be taken to achieve lower potential returns
(B) Potential return rises when higher risk is taken, and vice versa
(C) All investments must have the same level of risk and return
(D) Risk can be completely eliminated from all financial decisions

Ans :

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traditional partnership is not
(D) In an LLP, every partner is personally liable for the independent acts of another partner

Ans :

(C) An LLP is a separate legal entity, whereas a traditional partnership is not
A key distinction is that an LLP, established under the LLP Act, 2008, is recognized as a separate legal entity, distinct from its partners. In contrast, a traditional partnership firm has no separate legal status apart from its partners. This legal separation grants LLPs benefits like perpetual succession and limited liability.

Oct/Nov 2006

10. How does a Hindu Undivided Family (HUF) form of business come into existence?
(A) By birth in a Hindu family, not by a contractual agreement
(B) Through a formal contractual agreement between all family members
(C) By registering the family business under the Companies Act, 2013
(D) Through a special business license issued by the state government

Ans :

(A) By birth in a Hindu family, not by a contractual agreement
Unlike a partnership, which is formed through a contract, a Hindu Undivided Family (HUF) as a business entity comes into existence by operation of Hindu Law. Membership is acquired by birth into an undivided Hindu family. The business is owned by co-parceners, who are members of the family by birth.

May/June 2021

11. Who typically manages the business of a Hindu Undivided Family (HUF)?
(A) A professionally appointed Chief Executive Officer from outside the family
(B) All co-parceners equally through a formal democratic voting process
(C) A government-appointed administrator who oversees all operations
(D) The senior-most male member, who is known as the Karta

Ans :

(D) The senior-most male member, who is known as the Karta
The management of a HUF's business is traditionally vested in the senior-most male member of the family. This individual is referred to as the 'Karta' or 'Manager'. The Karta holds significant authority and is responsible for making business decisions on behalf of the entire family, with other members being co-parceners.

Oct/Nov 2010

12. What is the primary difference between an Association of Persons (AOP) and a Body of Individuals (BOI)?
(A) An AOP's sole purpose is earning income, while a BOI's is for non-income objectives
(B) An AOP can include artificial persons, while a BOI is comprised only of natural persons
(C) An AOP must be a registered entity, while a BOI is always an unregistered group
(D) There is no legal difference; the terms are used interchangeably for all tax purposes

Ans :

(B) An AOP can include artificial persons, while a BOI is comprised only of natural persons
The key distinction lies in the composition of their members. An Association of Persons (AOP) can include both natural persons (individuals) and artificial persons (like companies). In contrast, a Body of Individuals (BOI) is composed exclusively of natural persons (individuals) who join together for a common purpose, typically earning income.

May/June 2005

13. According to Section 2(20) of the Companies Act, 2013, how is a 'company' defined?
(A) An association of persons contributing to a common stock for a common purpose
(B) Any business entity with more than fifty members and limited liability status
(C) A company incorporated under this Act, or under any previous Company law
(D) A business exclusively formed for profit-making through mutual member assistance

Ans :

(C) A company incorporated under this Act, or under any previous Company law
The text provides the specific legal definition from Section 2(20) of the Companies Act, 2013. It defines a company simply as "A company incorporated under this Act, or under any previous Company law." This definition

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(A) Principals are managers; agents are shareholders
(B) Principals are customers; agents are suppliers
(C) Principals are bondholders; agents are employees
(D) Principals are shareholders; agents are managers

Ans :

(D) Principals are shareholders; agents are managers
In the context of a large corporation, the owners are the shareholders, who are considered the principals. They delegate the authority to run the company to the managers, who are therefore considered the agents. The managers are expected to act in the best interests of the shareholders, but their personal interests may sometimes conflict.

Oct/Nov 2023

42. Which of the following is NOT listed as a type of agency problem in a company?
(A) Shareholders vs. management
(B) Management vs. government regulators
(C) Shareholders vs. bondholders/other creditors
(D) Controlling shareholders vs. minority shareholders

Ans :

(B) Management vs. government regulators
The text explicitly lists four types of agency problems: Shareholders vs. management, Shareholders vs. bondholders/creditors, Controlling shareholders vs. minority shareholders, and Shareholders vs. other stakeholders (employees, customers, etc.). The relationship between management and government regulators, while important, is one of compliance and oversight, not typically classified as an agency problem in this context.

May/June 2016

43. Which of the following is a method suggested to mitigate agency problems in an organisation?
(A) Reducing operational transparency to the board of directors
(B) Guaranteeing fixed salaries regardless of company profitability
(C) Linking agent compensation to the principal's performance
(D) Removing all oversight on managerial decision-making authority

Ans :

(C) Linking agent compensation to the principal's performance
One of the key ways to mitigate agency problems is to align the interests of the agent (manager) with those of the principal (shareholder). This can be achieved by linking the agent's compensation to the firm's performance, such as through performance-based bonuses, profit sharing, or stock options, which reward the agent for increasing shareholder value.

Oct/Nov 2009

44. What is the main focus of 'Agency Theory' in explaining conflicts of interest?
(A) It focuses on the competitive conflict between a company and its market rivals
(B) It focuses on the interests of all stakeholders, including the community and suppliers
(C) It focuses on the relationship between a company and various government agencies
(D) It focuses primarily on the interest of the shareholders as principals

Ans :

(D) It focuses primarily on the interest of the shareholders as principals
The text clarifies that Agency Theory primarily describes the problems that occur when one party (the agent) represents another (the principal). It specifically highlights that Agency Theory mainly focuses on the interest of the shareholders, who are the principals in a corporate setting, and the potential conflicts with their agents, the managers.

May/June 2023

45. How does 'Stakeholder Theory' differ from 'Agency Theory'?
(A) Stakeholder theory includes the interests of all stakeholders, not just shareholders
(B) Stakeholder theory focuses only on maximizing returns for shareholders
(C) Stakeholder theory is a concept only applicable to small, proprietary businesses
(D) Stakeholder theory completely denies the existence of any conflicts of interest

Ans :

(A) Stakeholder theory includes the interests of all stakeholders, not just shareholders

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While Agency Theory primarily centers on the shareholder-manager relationship, Stakeholder Theory takes a broader view. It highlights the differing interests among all groups connected to the organization, including employees, investors, suppliers, customers, and the local community. It posits that business decisions should consider the interests of all these stakeholder groups.

Oct/Nov 2018

46. What is the primary focus of 'Business Ethics'?
(A) Maximizing corporate profits at any cost to the firm or society
(B) Classifying what is right and what is wrong for shareholders and stakeholders
(C) Adhering only to the minimum legal requirements of business operations
(D) Analyzing the impact of a firm's business on the global economy

Ans :

(B) Classifying what is right and what is wrong for shareholders and stakeholders
Business ethics is concerned with moral principles in a business context. It focuses on determining what is right and wrong in the conduct of business, specifically concerning the company's responsibilities and duties towards its shareholders and its broader group of stakeholders, such as employees, customers, and the community.

May/June 2007

47. How is 'Social Responsibility' distinguished from 'Business Ethics'?
(A) Social responsibility focuses on internal employee conduct, while ethics focuses on external impact
(B) Business ethics is a voluntary concept, while social responsibility is legally mandated
(C) Social responsibility focuses on the impact of a firm's business on the environment and community
(D) There is no significant difference; the two terms are used as synonyms

Ans :

(C) Social responsibility focuses on the impact of a firm's business on the environment and community
The text draws a distinction between the two concepts. While business ethics deals with the right and wrong of conduct towards all stakeholders, social responsibility has a more specific focus. It is primarily concerned with the impact that the firm's business operations and decisions have on the external environment and the community at large.

Oct/Nov 2025

48. According to the text, what is a key benefit for a company that practices high business ethics?
(A) It helps in attracting the best talent and retaining customers
(B) It can legally operate with fewer employees than competitors
(C) It is automatically exempted from paying all corporate taxes
(D) It can choose to ignore statutory and regulatory compliance

Ans :

(A) It helps in attracting the best talent and retaining customers
Practicing high business ethics enhances a company's reputation and brand value. This positive perception helps in attracting and retaining top talent, as people prefer to work for ethical companies. It also builds trust with customers, leading to repeat business, customer loyalty, and positive word-of-mouth, which helps increase market share.

May/June 2012

49. Which of the following is listed as a broad principle of a business's code of conduct?
(A) Profit Maximization
(B) Market Domination
(C) Promise-Keeping
(D) Competitive Exclusion

Ans :

(C) Promise-Keeping
The text provides a comprehensive list of broad principles that can be part of a code of conduct or ethics in business. Among the principles listed are Personal responsibility, Honesty, Integrity, Trustworthiness, Loyalty, Fairness, and Promise-Keeping. Promise-keeping refers to the ethical obligation to honor commitments and agreements.

Oct/Nov 2014

50. According to Shri Narayan Murthy, what is the definition of "Social responsibility"?
(A) To create maximum shareholder value while

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being fair to all stakeholders
(B) To exclusively focus on environmental protection initiatives above all else
(C) To donate a fixed percentage of annual revenue to designated charities
(D) To prioritize community welfare and employee benefits over shareholder returns

Ans :

(A) To create maximum shareholder value while being fair to all stakeholders
The text quotes Shri Narayan Murthy's definition of social responsibility. He defines it as the goal "to create maximum shareholders value, working under the circumstances, where it is fair to all its stakeholders, workers, consumers, the community, government and the environment." This definition emphasizes balancing shareholder value with fairness to all other stakeholders.

May/June 2019

51. The European Union Commission's definition of CSR describes it as a concept where companies integrate social and environmental concerns into their business operations on what basis?
(A) On a mandatory basis as strictly required by international law
(B) Only when specifically directed to do so by a court order
(C) Only for their international operations in developing countries
(D) On a voluntary basis, going beyond legal compliance

Ans :

(D) On a voluntary basis, going beyond legal compliance
The European Union Commission's definition of Corporate Social Responsibility (CSR) highlights its voluntary nature. It is defined as "a concept whereby companies integrate social and environment concerns in their business operations and in their interaction with their stakeholder on a voluntary basis." This implies going beyond legal obligations to benefit society.

Oct/Nov 2006

52. Corporate social responsibility is traditionally grouped into four categories. Which of the following is NOT one of those categories?
(A) Environmental
(B) Technological
(C) Philanthropic
(D) Economic

Ans :

(B) Technological
The text states that corporate social responsibility is traditionally grouped into four distinct categories. These are: environmental responsibility (e.g., recycling), philanthropic responsibility (e.g., donation camps), ethical responsibility (fair business practices), and economic responsibility (being profitable while acting ethically). Technological is not listed as one of these traditional categories.

May/June 2021

53. According to Section 135 of the Companies Act, 2013, what is the statutory CSR spending requirement for applicable companies in India?
(A) At least 1% of average net profits of the three previous financial years
(B) A fixed amount of Rs. 1 crore, irrespective of the company's size or profits
(C) At least 2% of average net profits of the three previous financial years
(D) At least 5% of the net profit generated during the current financial year

Ans :

(C) At least 2% of average net profits of the three previous financial years
The legal aspects of CSR in India are governed by Section 135 of the Companies Act, 2013. This section mandates that most companies meeting certain criteria must spend at least 2% of their average net profits, calculated over the three immediately preceding financial years, on CSR activities during the current financial year.

Oct/Nov 2010

54. Where must a company disclose the details of its CSR activities as per the Companies Act, 2013?
(A) In a press release distributed to all major media outlets
(B) In an internal memorandum circulated only to employees
(C) In a confidential report submitted to the Ministry of Finance
(D) In the Annual report of the Board of Directors

Ans :

(D) In the Annual report of the Board of Directors
The statutory obligations under Section 135 of the Companies Act, 2013, require transparency

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in CSR spending. Companies are mandated to disclose the details of the CSR activities they have undertaken. This disclosure must be made separately in the Annual report prepared by the Board of Directors for the shareholders and public.

May/June 2005

55. Why does the organisation of the finance function vary between different businesses?
(A) Because it is tailored to each firm's unique size and objectives
(B) Because all businesses are legally required to adopt an identical structure
(C) Because a government agency assigns a specific structure to each company
(D) Because the structure is determined solely by the number of employees

Ans :

(A) Because it is tailored to each firm's unique size and objectives
There is no one-size-fits-all structure for a finance function. Each business is unique in its size, model, structure, and objectives. Consequently, the organisation of the finance function is tailored to the specific needs of each company. A large, complex company will have a more specialized finance structure than a small business.

Oct/Nov 2022

56. When structuring a finance team, what is a potential drawback of outsourcing certain finance tasks?
(A) It always costs significantly more than performing the task internally
(B) The external agency can be slow and may not understand the business properly
(C) It prevents the internal team from focusing on core strategic activities
(D) It is illegal in most jurisdictions to outsource any accounting or finance work

Ans :

(B) The external agency can be slow and may not understand the business properly
While outsourcing can be beneficial, the text points out its potential drawbacks. A key challenge is that an external agency might be slow in its response and may lack a deep, proper understanding of the specific business's nuances and needs. This can lead to inefficiencies and decisions that are not perfectly aligned with the company's strategy.

May/June 2018

57. What is a key consideration mentioned for structuring the right finance team?
(A) Ensuring team members have no inclination to collaborate with the wider business
(B) Avoiding the use of any new software tools in order to reduce operational costs
(C) Focusing exclusively on financing activities while ignoring planning and control
(D) Assessing if the team needs external help for expert support

Ans :

(D) Assessing if the team needs external help for expert support
One of the critical questions to consider when structuring a finance team is about capabilities and support. A firm must assess whether it has the necessary expert support within its own team or if it needs to seek external support for specialist tasks like tax matters. This decision impacts the team's focus and efficiency.

Oct/Nov 2016

58. What common factor links the fields of economics and finance?
(A) Money is a common factor in both disciplines
(B) They both focus exclusively on stock market performance
(C) They both are primarily concerned with business law
(D) They both study the historical development of political systems

Ans :

(A) Money is a common factor in both disciplines
The text states that money is a common factor in both economics and finance, leading many to see them as two sides of the same coin. Both fields deal with related topics like interest rates and marginal cost. This shared focus on money and its management is a fundamental link between the two areas.

May/June 2014

59. What is a key difference in focus between Economics and Finance?
(A) Economics is a more practical field, while finance is more theoretical
(B) Finance studies supply and demand, while

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economics studies banks and credit
(C) Economics studies broader aspects, while finance focuses on managing a firm's funds
(D) There is no difference in focus; they are identical and interchangeable fields

Ans :

(C) Economics studies broader aspects, while finance focuses on managing a firm's funds
While related, their scope differs. Economics takes a broader view, studying aspects like the production and consumption of goods and services in local and global markets. Finance is narrower, focusing specifically on the techniques and tools for sourcing and managing money to achieve the objectives of a particular organisation efficiently.

Oct/Nov 2007

60. How are financial decisions in an organisation recorded?
(A) They are recorded through the process of accounting
(B) They are recorded through the process of marketing
(C) They are recorded by the human resources department
(D) They are not recorded but are communicated verbally

Ans :

(A) They are recorded through the process of accounting
Financial decisions, once implemented, result in financial transactions. These transactions, such as a public issue of equity or the purchase of a machine, are systematically recorded in the books of account. The process of recording, analyzing, and summarizing these transactions is the core function of accounting.

May/June 2025

61. Financial decisions are made for the future, but what are they mostly based on?
(A) The personal opinions and intuition of the finance manager
(B) The marketing department's unverified sales forecasts
(C) The prevailing general economic climate and sentiment only
(D) The historical data provided by the accounting function

Ans :

(D) The historical data provided by the accounting function
Although financial decisions are forward-looking, they are not made in a vacuum. They are heavily based on the historical financial data provided by the accounting function. A comprehensive and correct data backbone, such as that found in the balance sheet and P&L account, is essential for making sound financial decisions.

Oct/Nov 2019

62. Which of the following is an example of accounting data being used for a financial decision?
(A) Using customer feedback surveys to design a completely new product
(B) Using the P&L account to decide on dividend payment and retention of profits
(C) Using employee performance reviews to decide on internal promotions
(D) Using market research reports to set up a new advertising campaign

Ans :

(B) Using the P&L account to decide on dividend payment and retention of profits
The text provides specific examples of this link. The balance sheet and Profit & Loss (P&L) accounts, which are outputs of the accounting process, form the basis for crucial financial decisions. These include deciding how much dividend to pay out to shareholders and how much profit to retain for future growth.

May/June 2009

63. What has been a major consequence of the relaxation in industrial licensing in India for finance managers?
(A) It has made the selection of a new project significantly less challenging
(B) It has completely eliminated the need for any kind of project evaluation
(C) It has resulted in increased competition, making project selection more challenging
(D) It has shifted the focus of finance managers completely away from project selection

Ans :

(C) It has resulted in increased competition, making project selection more challenging

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I. Agency theory mainly focuses on the interest of shareholders.
II. Stakeholder theory includes the interests of all stakeholders, such as employees, suppliers, and the community.
III. Agency theory and Stakeholder theory are identical in their scope and focus.

Which of the above statements is/are correct?
(A) Only I
(B) Only I and II
(C) Only II and III
(D) All I, II, and III

Ans :

(B) Only I and II
The text draws a clear distinction. Agency theory is described as mainly focusing on the interests of shareholders (the principals). In contrast, Stakeholder theory is presented as having a broader scope, highlighting the interests of all groups within and outside the organisation (employees, investors, suppliers, community, etc.). Therefore, statement III is incorrect.

May/June 2024

73. Consider the following activities:
1. Estimating capital requirements
2. Deciding on sources of funds
3. Working capital management
4. Decision of dividend/retained profit

All of the above are primarily related to which function in a firm?
(A) Human Resource Management
(B) Marketing Management
(C) Financial Management
(D) Operations Management

Ans :

(C) Financial Management
All four activities listed—estimating capital needs, deciding on funding sources, managing current assets and liabilities (working capital), and determining dividend policy—are explicitly described in the text as core functions and decisions that fall under the scope of financial management. They are central to managing a firm's financial resources effectively.

Oct/Nov 2008

74. **Assertion (A) :** In a sole proprietorship, the profit is taxed as the personal income of the owner.
Reason (R) : There is no legal distinction between the owner and the firm in a sole proprietorship.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
The text establishes that a sole proprietorship lacks a separate legal identity from its owner. Because the firm and owner are legally one and the same, the profits generated by the business are treated as the proprietor's personal income for tax purposes. Thus, the reason correctly explains the assertion.

May/June 2006

75. **Assertion (A) :** A finance manager may decide to dispose of old assets even if they are functional.
Reason (R) : The return from old assets may be lower than the opportunity cost of deploying the capital elsewhere.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
The principle of opportunity cost applies to retaining old assets. If the return generated by an old asset is less than the return that could be earned by selling it and investing the proceeds in a new, better-returning asset (the opportunity cost), it is a sound financial decision to dispose of the old asset.

Oct/Nov 2017

76. **Assertion (A) :** An investment in junk bonds involves high risk.
Reason (R) : Junk bonds offer a high yield because of a low market rate and a high probability of default.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).

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Oct/Nov 2005

68. Which of the following statements about financial decisions in a firm is correct?
(A) Techniques like IRR and NPV are used for investment decisions on long-term assets
(B) A high proportion of debt in the capital structure always guarantees higher profitability
(C) Working capital management is primarily concerned with long-term investment decisions
(D) The decision on dividend and retained profit is taken without considering shareholder interests

Ans :

(A) Techniques like IRR and NPV are used for investment decisions on long-term assets
The appraisal of long-term investment proposals, or capital budgeting, requires specific analytical tools. The text explicitly mentions Internal Rate of Return (IRR) and Net Present Value (NPV) as techniques used for these decisions to assess the return on capital employed and select the best risk-adjusted return projects.

May/June 2020

69. Identify the incorrect statement regarding the fundamental principles of finance.
(A) The principle of diversification suggests spreading risk over many investments
(B) The risk and return principle implies that higher risk is normally associated with higher return
(C) The time value of money principle exists only because of inflation
(D) Opportunity cost is the return given up on the next best alternative investment

Ans :

(C) The time value of money principle exists only because of inflation
The text explicitly states that the time value of money is not only because of inflation. A crucial reason is that money has earning power; it can be invested to generate returns. This potential to earn interest is a fundamental component of the principle, separate from the eroding effect of inflation on purchasing power.

Oct/Nov 2015

70. Consider the following statements about business organisations:
Statement I : In a partnership firm, the liability of each partner is unlimited.
Statement II : In a Limited Liability Partnership (LLP), all partners have limited liabilities.
Which of the following is correct?
(A) Only Statement I is correct.
(B) Only Statement II is correct.
(C) Both Statement I and Statement II are correct.
(D) Both Statement I and Statement II are incorrect.

Ans :

(C) Both Statement I and Statement II are correct.
The text clearly distinguishes between the two forms. It states that in a traditional partnership firm, the liability of each partner is unlimited. It then introduces the LLP as a form where some or all partners have limited liabilities, which is a defining feature that gives it elements of a limited company.

May/June 2013

71. With regard to financial management, consider the following statements:
Statement I : Organic growth means acquiring the businesses of other firms.
Statement II : Inorganic growth means expansion by creating additional capacity and adding more fixed assets.
Which of the following is correct?
(A) Statement I is correct, but Statement II is incorrect.
(B) Statement II is correct, but Statement I is incorrect.
(C) Both Statement I and Statement II are correct.
(D) Both Statement I and Statement II are incorrect.

Ans :

(D) Both Statement I and Statement II are incorrect.
The statements have the definitions reversed. Organic growth refers to internal expansion by creating additional capacity and adding fixed assets. Inorganic growth, on the other hand, refers to external expansion achieved by acquiring other businesses through mergers and acquisitions. Therefore, both statements as presented are incorrect.

Oct/Nov 2021

72. Examine the following statements related to conflicts of interest:

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(B) Because it directly increases the firm's overall profitability
(C) Because it violates statutory liquidity ratio requirements for banks
(D) Because it automatically leads to an increase in current liabilities

Ans :

(A) Because it is a waste of a precious resource that could be invested
The excerpt highlights the trade-off between liquidity and profitability. While liquidity is important, holding excessive idle cash is inefficient because cash is a "precious resource." Idle cash earns no return, representing a missed opportunity to invest it in profitable ventures. This inefficient use of resources negatively impacts overall profitability.

May/June 2011

81. What is the primary distinction between Agency Theory and Stakeholder Theory as described in the excerpt?
(A) Agency Theory is about external conflicts, while Stakeholder Theory is about internal conflicts
(B) Agency Theory promotes conflict, while Stakeholder Theory promotes harmony
(C) Agency Theory applies to non-profits, while Stakeholder Theory applies to for-profit companies
(D) Agency Theory has a narrow focus on shareholders, while Stakeholder Theory has a broad focus

Ans :

(D) Agency Theory has a narrow focus on shareholders, while Stakeholder Theory has a broad focus
The excerpt explicitly states that Agency Theory "mainly focuses on the interest of shareholders." In contrast, it describes Stakeholder Theory as highlighting differences of interest among various internal groups (employees, investors) and also "outside stakeholders like the local community." This clearly indicates a difference in the breadth of focus between the two theories.

Oct/Nov 2020

82. Based on the excerpt, how is the mandatory CSR spending for a company calculated?
(A) It is 2% of the net profit of the current financial year
(B) It is at least 2% of the average net profits of the preceding three financial years
(C) It is 2% of the total revenue of the last financial year
(D) It is a fixed 2% of the company's total share capital

Ans :

(B) It is at least 2% of the average net profits of the preceding three financial years
The excerpt is very specific about the calculation basis for statutory CSR spending. It is not based on the current year's profit or on revenue or capital. The rule requires calculating the average of the net profits made during the three immediately preceding financial years and then spending at least 2% of that average amount.

May/June 2022

83. According to the excerpt, what is the core focus of the field of finance?
(A) Studying consumer behavior and global macroeconomic market trends
(B) Analyzing the production and consumption of goods and services on a macro level
(C) Using techniques and tools to manage money for achieving an organisation's objectives
(D) Examining historical economic theories and their philosophical development

Ans :

(C) Using techniques and tools to manage money for achieving an organisation's objectives
The excerpt clearly differentiates finance from economics by defining its focus. It states that the "focus of finance is on using the techniques and tools of managing money to achieve the business objectives of an organisation in an efficient manner." This highlights its practical, tool-oriented, and organisation-specific nature compared to the broader scope of economics.

Oct/Nov 2023

84. Based on the excerpt, what are two significant outcomes of a company applying high ethical standards?
(A) Reduced tax liabilities and access to special government subsidies
(B) The ability to charge higher prices and reduce overall product quality
(C) Lower marketing costs and a guaranteed reduction in legal disputes
(D) Higher employee productivity and increased

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(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
The text uses junk bonds as an example of a high-risk investment. The reason for the high risk is the high probability of default. To compensate investors for taking on this significant risk, these bonds must offer a high yield, which is often a result of being traded at a low price (low market rate).

May/June 2008

77. Match the form of business organisation in List-I with its corresponding characteristic in List-II.
List-I (Form of Business)
P. Sole Proprietary
Q. Partnership Firm
R. Limited Liability Partnership
S. Company
List-II (Characteristic)
1. Has a separate legal status and one partner is not liable for another's act.
2. Formed by incorporation under the Companies Act, 2013 or previous law.
3. No legal distinction between the owner and the firm.
4. Governed by an Act of 1932 and has a maximum of 50 members.

Code:
(A) P-3, Q-4, R-1, S-2
(B) P-4, Q-3, R-2, S-1
(C) P-3, Q-1, R-4, S-2
(D) P-2, Q-4, R-1, S-3

Ans :

(A) P-3, Q-4, R-1, S-2
A Sole Proprietary firm has no legal distinction from its owner (P-3). A Partnership Firm is governed by the 1932 Act and limited to 50 partners (Q-4). An LLP is a separate legal entity where partners have limited liability (R-1). A Company is an entity incorporated under company law (S-2).

Oct/Nov 2013

78. Match the financial principle in List-I with its correct description in List-II.
List-I (Principle)
P. Time Value of Money
Q. Diversification
R. Hedging
S. Opportunity Cost
List-II (Description)
1. Spreading risk by not putting all eggs in one basket.
2. A rupee today is worth more than a rupee tomorrow due to earning power.
3. The return foregone from the next best alternative.
4. Meeting long-term fund needs from long-term sources.

Code:
(A) P-1, Q-2, R-3, S-4
(B) P-2, Q-1, R-4, S-3
(C) P-3, Q-4, R-1, S-2
(D) P-2, Q-3, R-4, S-1

Ans :

(B) P-2, Q-1, R-4, S-3
Time Value of Money states a rupee today is worth more than one tomorrow (P-2). Diversification involves spreading investments to reduce risk (Q-1). Hedging (asset-liability management) involves matching the tenor of funds with assets (R-4). Opportunity Cost is the return given up on the next-best alternative (S-3).

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May/June 2015

79. Based on the provided definition of a partnership, which element is NOT explicitly required?
(A) An agreement between the persons
(B) The business must be carried on by all partners simultaneously
(C) The objective of the business must be to share profits
(D) There must be at least two persons

Ans :

(B) The business must be carried on by all partners simultaneously
The definition clearly states the business can be "carried on by all or any of them acting for all." This concept of mutual agency means that it is not necessary for all partners to be actively involved in the day-to-day operations. One partner can act on behalf of all others, making this a flexible arrangement.

Oct/Nov 2012

80. According to the excerpt, why is holding "too much idle cash" considered an inefficiency?
(A) Because it is a waste of a precious resource that could be invested

The post-liberalization era in India saw a relaxation in industrial licensing. This opened up the market and led to a significant increase in competition. For a finance manager, this heightened competition has made the task of selecting a viable and profitable project more difficult and challenging than before.

Oct/Nov 2011

64. What was the impact of the abolition of the Capital Issues (Control) Act on the role of the finance manager?

(A) It made it functionally impossible for companies to raise new equity capital
(B) It completely removed all regulations and oversight related to raising capital
(C) It significantly reduced the importance of the finance manager in raising equity
(D) It expanded capital markets but created challenges with stricter disclosure rules

Ans :

(D) It expanded capital markets but created challenges with stricter disclosure rules
The abolition of the Capital Issues (Control) Act was a major reform that eased the process of raising resources and helped the capital market to expand. However, this was accompanied by the introduction of more stringent investor protection rules and disclosure requirements, which created new challenges and responsibilities for the finance manager.

May/June 2010

65. What difficulty has arisen for finance managers in raising long-term debt following the disappearance of Development Financial Institutions (DFIs)?

(A) Raising long-term resources has become difficult, especially for infrastructure projects
(B) Commercial banks are now completely unwilling to provide any form of loans
(C) The cost of short-term debt and working capital has become prohibitively high
(D) There are no prudential norms for banks, leading to an excess of reckless lending

Ans :

(A) Raising long-term resources has become difficult, especially for infrastructure projects
Erstwhile Development Financial Institutions (DFIs) were a key source of long-term project finance. Their disappearance has created a void. Commercial banks, which are now major lenders, face asset-liability mismatch issues when providing long-term loans. This has made it more difficult for finance managers to raise long-term debt, particularly for large infrastructure projects.

Oct/Nov 2024

66. Identify the incorrect statement regarding a Sole Proprietary firm.

(A) It is a type of firm owned and run by one person
(B) There is a legal distinction between the owner and the firm
(C) The profit of the firm is taxed as the personal income of the proprietor
(D) It faces a limitation of capital as the proprietor's resources are limited

Ans :

(B) There is a legal distinction between the owner and the firm
A defining characteristic of a sole proprietorship is that there is no legal distinction between the owner (the proprietor) and the business entity. They are considered one and the same in the eyes of the law. This is why the owner has unlimited liability and the firm's profits are taxed as personal income.

May/June 2017

67. Identify the correct statement regarding a Limited Liability Partnership (LLP).

(A) It is primarily governed by the Indian Partnership Act, 1932
(B) In an LLP, one partner is always liable for the independent acts of another partner
(C) An LLP is a legal entity with a separate status from its partners
(D) Registration of an LLP is typically done with the Registrar of Firms

Ans :

(C) An LLP is a legal entity with a separate status from its partners
An LLP, introduced by the LLP Act of 2008, is a distinct legal entity, separate from its partners, much like a company. This is a key difference from a traditional partnership. Consequently, one partner is not liable for another's actions, and it is registered with the Ministry of Corporate Affairs, not the Registrar of Firms.

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customer loyalty

Ans :

(D) Higher employee productivity and increased customer loyalty

The excerpt directly links high ethical standards to specific positive outcomes. It mentions that ethical treatment of employees leads to "high productivity and low attrition rates." It also states that ethical treatment of customers makes them "repeat customers" who build an "ongoing relationship," which is a form of customer loyalty.

May/June 2016

85. What defines an investment decision as 'Capital Budgeting' according to the excerpt?

(A) The benefits from the investment are expected to be available for a long time
(B) The decision involves only a very small, insignificant amount of money
(C) The investment is in short-term, highly liquid assets like cash
(D) The decision is made exclusively by the marketing department of the firm

Ans :

(A) The benefits from the investment are expected to be available for a long time

The excerpt characterizes a capital budgeting decision by the nature of its outcomes. It is a choice regarding a capital asset or investment proposal "whose benefits are likely to be available in future for a long time." This long-term horizon of benefits is the key feature that distinguishes it from short-term operational decisions.

Oct/Nov 2009

86. What is the legal status of a registered co-operative society as per the excerpt?

(A) It has the same legal identity as its collective members
(B) It is a separate legal entity, distinct and independent of its members
(C) It is not recognized by law as a valid or enforceable legal entity
(D) It cannot own assets or be a party to a legal lawsuit

Ans :

(B) It is a separate legal entity, distinct and independent of its members

The excerpt explicitly states that a registered co-operative society is "recognized as a separate legal entity by law" and acquires an "identity quite distinct and independent of its members." The consequences of this status, such as the ability to own assets and sue or be sued, are also mentioned, reinforcing its separate legal existence.

May/June 2023

87. According to the excerpt, why do banks face an "asset-liability mismatch" when providing long-term loans?

(A) Because they have a structural excess of long-term deposits
(B) Because they are legally prohibited from funding infrastructure projects
(C) Because the DFIs took all the long-term assets with them
(D) Because their liabilities (deposits) are typically short-term while the asset (loan) is long-term

Ans :

(D) Because their liabilities (deposits) are typically short-term while the asset (loan) is long-term

The issue of asset-liability mismatch for banks arises from the different time horizons of their sources and uses of funds. Banks' primary liabilities are customer deposits, which are mostly short to medium-term. Providing a very long-term loan (an asset) with these short-term funds creates a mismatch, exposing the bank to significant liquidity and interest rate risks.

Oct/Nov 2018

88. What does the excerpt imply about the optimal capital structure?

(A) The optimal capital structure involves a balance between the risks of high debt and the missed opportunities of low debt
(B) The best and most profitable capital structure is one that consists of 100% debt
(C) The safest and therefore best capital structure is one that consists of 0% debt
(D) Capital structure is a minor decision that has no real impact on a firm's profitability or viability

Ans :

(A) The optimal capital structure involves a balance between the risks of high debt and the missed opportunities of low debt

The excerpt presents two extremes. High debt is risky and can threaten viability, while low debt

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leads to under-utilization of profit potential (financial leverage). This implies that the ideal or optimal capital structure is not at either extreme but is a carefully considered balance that maximizes return without taking on excessive risk.

May/June 2007

89. A startup company, "Innovatech," needs to fund a new research project. The finance manager is evaluating two options: issuing more equity shares to new investors or taking a large term loan from a bank. This decision-making process is a core part of:
(A) Working Capital Management
(B) Dividend Policy
(C) Deciding the Capital Structure
(D) Financial Control

Ans :

(C) Deciding the Capital Structure
This scenario involves choosing between debt (term loan) and equity (issuing shares) to finance a project. This choice directly pertains to deciding the capital structure or composition of the firm's funds. The finance manager is weighing the mix of debt and equity, which is a crucial financial decision affecting risk and return.

Oct/Nov 2025

90. A finance manager at "Global Exports Ltd." has Rs. 10 crore to invest. He can either put it in a government bond yielding 6% or invest in a new overseas project with a potential return of 18% but a significant risk of failure. The manager's deliberation between these two options best exemplifies the:
(A) Risk-Return Trade-off
(B) Agency Problem
(C) Principle of Diversification
(D) Asset-Liability Mismatch

Ans :

(A) Risk-Return Trade-off
The case presents a classic financial dilemma. The government bond offers a low but safe return (low risk, low return). The overseas project offers a much higher potential return but comes with a high risk of failure. The manager must weigh the potential for higher rewards against the increased risk, which is the essence of the risk-return trade-off.

May/June 2012

91. The CEO of "Prestige Corp," whose bonus is tied to the company's annual reported profit, decides to postpone a major, necessary equipment upgrade to the next financial year. This will boost the current year's profit but may harm long-term productivity. This situation is a classic example of:
(A) A Capital Budgeting success
(B) Effective Social Responsibility
(C) A Hedging Strategy
(D) An Agency Problem

Ans :

(D) An Agency Problem
This is a clear conflict of interest between the agent (CEO) and the principals (shareholders). The CEO is making a decision to maximize his personal bonus (short-term profit) at the potential expense of the company's long-term health and shareholder value. This misalignment of interests is the core of an agency problem.

Oct/Nov 2014

92. "GreenEnergy Corp." decides to invest in technology that reduces its factory emissions, even though the investment exceeds the minimum legal requirement. The company also funds a local community park. These actions fall under the purview of:
(A) Capital Structure Optimisation
(B) Business Ethics and Social Responsibility
(C) Working Capital Management
(D) Risk-Return Trade-off

Ans :

(B) Business Ethics and Social Responsibility
The company is voluntarily going beyond its legal obligations to benefit the environment (reducing emissions) and the local community (funding a park). These actions are not primarily driven by immediate profit or legal compulsion but by a sense of duty towards society and the environment, which are key components of social responsibility.

May/June 2019

93. An investor has Rs. 1,00,000. Instead of investing the entire amount in the stock of a single IT company, she decides to invest Rs. 20,000 each in an IT stock, a pharma stock, a bank stock, a government bond, and gold. This investment

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strategy is an application of which financial principle?
(A) Time Value of Money
(B) Liquidity and Return
(C) Diversification
(D) Opportunity Cost

Ans :

(C) Diversification
The investor is deliberately avoiding concentrating her funds in a single asset. By spreading her investment across different asset classes (stocks from various sectors, bonds, gold), she is applying the principle of diversification. The goal is to reduce the overall risk of her portfolio, as a loss in one investment might be offset by gains in another.

Oct/Nov 2006

94. A firm needs to finance a new factory with a 20-year lifespan. The finance manager insists on funding it with a 20-year term loan or equity, rather than using the company's short-term cash credit line from a bank. This manager is adhering to the principle of:
(A) Diversification
(B) Opportunity Cost
(C) Liquidity and Return
(D) Reducing asset-liability mismatch/Hedging

Ans :

(D) Reducing asset-liability mismatch/Hedging
The manager is matching the maturity of the asset (a 20-year factory) with the maturity of the liability (a 20-year loan or perpetual equity). This is a direct application of the hedging or asset-liability matching principle, which states that long-term fund requirements should be met from long-term sources to avoid refinancing risk and liquidity problems.

May/June 2021

95. A large manufacturing company's finance department is split into two divisions. One division handles budgeting, profit planning, and financial reporting. The other handles raising funds, managing cash, and investment decisions. This departmental structure reflects the application of which building block of modern finance?
(A) Organising and Directing
(B) Controlling
(C) Decision Making
(D) Planning

Ans :

(A) Organising and Directing
This case describes the process of structuring the finance function to implement decisions effectively. By creating separate functional heads for Planning/Accounting/Control activities and for Financing/Investment activities, the company is building an organizational capability to execute its financial strategy. This is a clear example of the 'Organising and Directing' block of modern finance.

Oct/Nov 2010

96. "BuildIt Corp" is a construction company. Its finance manager uses the company's balance sheet and P&L account to decide on acquiring new machinery and to determine how much profit should be retained for future projects. This scenario illustrates the close relationship between:
(A) Finance and Economics
(B) Finance and Accounting
(C) Finance and Marketing
(D) Finance and Human Resources

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Ans :

(B) Finance and Accounting
The case shows a financial manager making future-oriented decisions (acquiring assets, retaining profits) based on historical data. The balance sheet and P&L account are key outputs of the accounting process. This direct use of accounting information as the backbone for financial decision-making highlights the very close and interconnected relationship between the two functions.

May/June 2005

97. Post the 1991 economic reforms in India, a finance manager at an automobile company finds it much harder to choose new projects because numerous domestic and international players have entered the market. This increased difficulty in project selection is a direct result of:
(A) The relaxation in industrial licensing leading to increased competition
(B) The abolition of the Capital Issues (Control) Act
(C) The disappearance of Development Financial Institutions (DFIs)
(D) The introduction of more stringent CSR

(A) Diversification

The text explicitly links the principle of diversification to the idiom, "never put all your eggs in one basket." This principle implies that risk should be spread over many investments instead of being concentrated in just one or two, so that the failure of a single investment does not lead to a total loss.

Oct/Nov 2023

126. A company's finance team is considering whether to buy a standardized accounting software package or develop a custom one. They are concerned that the cost of customization might be too high. This reflects which consideration in structuring a finance team?

(A) Outsourcing benefits and drawbacks
(B) The appropriate balance between software tools and individual capabilities
(C) The need for internal vs. external expert support
(D) The team's inclination to collaborate with the wider business

Ans :

(B) The appropriate balance between software tools and individual capabilities

This scenario deals with the choice of tools to simplify tasks. The text specifically mentions the need to "consider new software tools carefully to ensure that the customisation costs are not prohibitive" while discussing the balance between software and individual capabilities. The team is weighing the cost and benefit of a standard tool versus a custom one.

May/June 2016

127. If a firm's actual return on an investment is less than its forecast return, this possibility is defined as:

(A) Profit
(B) Liquidity
(C) Opportunity Cost
(D) Risk

Ans :

(D) Risk

The text provides a clear definition of risk in the context of the risk-return trade-off. It is defined as "the possibility that the actual return from an investment will be less than the forecast return." This uncertainty of outcome is the essence of investment risk.

Oct/Nov 2009

128. What is the main characteristic of a "One-Person Company" as permitted by the Companies Act, 2013?

(A) It is a company that has only one person as its member
(B) It is a company that has only one employee
(C) It is a company that can only operate for one year
(D) It is a company that can only sell one product

Ans :

(A) It is a company that has only one person as its member

The text, while discussing the definition of a company under the Companies Act, 2013, mentions that the Act "also permits formation of 'One-Person Company' which has only one person as its member." This allows a single promoter to enjoy the benefits of a corporate structure, like limited liability.

May/June 2023

129. The finance function that involves balancing cash inflows and outflows to ensure adequate liquidity and discounting cash inflows to their present value is based on the:

(A) Principle of Diversification
(B) Principle of Integrity
(C) Principle of Cash Flow
(D) Principle of Accountability

Ans :

(C) Principle of Cash Flow

The text describes the cash flow principle as having two aspects. The first is balancing inflows and outflows for liquidity. The second is applying the time value of money concept by discounting future cash flows. Both aspects are central to the cash flow principle in financial management.

Oct/Nov 2018

130. Examine the following statements:

I. Financial management means applying management principles to financial resources.
II. The choice of business organisation form can have tax implications if changed later.
III. A partnership firm has a separate legal status apart from its partners.

Which of the above statements is/are correct?

(A) I and II only
(B) Only I

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ethics, guiding the company's interactions with its employees, customers, and other stakeholders.

Oct/Nov 2007

102. Which statement accurately describes the legal status of a Hindu Undivided Family (HUF) for tax purposes?
(A) It is not recognized as a separate taxable entity by tax law
(B) It is considered a separate entity and is taxed separately
(C) Its income is always clubbed with the Karta's personal income
(D) It is taxed under the exact same rules as a partnership firm

Ans :

(B) It is considered a separate entity and is taxed separately
The text explicitly states that "For the sake of income tax, the HUF is considered as a separate entity and is taxed separately." This means the HUF has its own PAN card and files its own tax returns, distinct from the individual returns of its members, including the Karta.

May/June 2025

103. In the modern approach to finance, which block involves examining plans for their viability and making investment, financing, and profit distribution choices?
(A) Planning
(B) Organising and Directing
(C) Decision making
(D) Controlling

Ans :

(C) Decision making
The text describes 'Decision making' as the block where plans are examined for viability, considering business environment constraints and firm capabilities. It explicitly states that the main decisions in a firm are investment decisions, financing decisions, and profit distribution decisions, which are all part of this 'Decision making' building block.

Oct/Nov 2019

104. What is the primary purpose of financial techniques like ratio analysis, costing, and budgetary control?
(A) To raise long-term funds from capital markets
(B) To appraise and select new investment proposals
(C) To decide the firm's optimal capital structure
(D) To serve as tools for Financial Control

Ans :

(D) To serve as tools for Financial Control
The text mentions that for the purpose of Financial Control—which involves continuously monitoring activities to identify inefficiency and take corrective action—many techniques are available. It then explicitly lists ratio analysis, costing, and budgetary control as examples of these techniques used for control and monitoring purposes.

May/June 2009

105. A firm's management wants to sustain business operations and ensure it can meet its day-to-day obligations. Which aspect of working capital management is most critical for this objective?
(A) Liquidity
(B) Profitability
(C) Growth
(D) Diversification

Ans :

(A) Liquidity
The text states, "Liquidity is an important requirement for sustaining the operations of business." While profitability is the ultimate goal, having sufficient liquidity (cash and cash equivalents) is essential to pay suppliers, employees, and other short-term creditors, thereby ensuring the business can continue to operate without interruption.

Oct/Nov 2011

106. Identify the incorrect pair from the following.
(A) Sole Proprietary - Unlimited Liability
(B) LLP - Governed by Partnership Act, 1932
(C) Company - Separate Legal Entity
(D) HUF - Managed by Karta

Ans :

(B) LLP - Governed by Partnership Act, 1932
A Limited Liability Partnership (LLP) is a newer concept introduced in India by the Limited Liability Partnership Act, 2008. It is not governed by the traditional Indian Partnership Act, 1932. The 1932 Act governs traditional partnership firms, which have different features, such as unlimited liability for partners.

NODIA

May/June 2010

107. Consider the following statements about the relationship between Finance and Accounting:
Statement I : Financial decisions are for the future and are based on historical data provided by accounting.
Statement II : Accounting involves broader aspects of planning and control, while financial management mainly involves recording data.
Which of the following is correct?
(A) Only Statement II is correct.
(B) Both Statement I and Statement II are correct.
(C) Both Statement I and Statement II are incorrect.
(D) Only Statement I is correct.

Ans :

(D) Only Statement I is correct.
Statement I is correct as financial decisions are forward-looking but rely on past data from accounting records. Statement II is incorrect because it reverses the roles. Financial management involves the broader aspects of planning and control, while accounting is primarily concerned with the recording, analysis, and presentation of financial data.

Oct/Nov 2024

108. The principle that "long-term fund requirements should be met from long-term sources and short-term fund requirements should be met from short-term sources" is known as:
(A) Reducing asset-liability mismatch/Hedging
(B) Time Value of Money
(C) Diversification
(D) Risk and Return

Ans :

(A) Reducing asset-liability mismatch/Hedging
This statement is the exact definition provided for the principle of reducing asset-liability mismatch, also referred to as hedging. It is a fundamental principle of prudent financial management aimed at aligning the maturity profile of a firm's assets (uses of funds) with its liabilities (sources of funds) to manage risk.

May/June 2017

109. Which of the following is an example of a philanthropic activity under Corporate Social Responsibility?
(A) Reducing plastic waste in the production process
(B) Ensuring fair pricing and good quality for all products
(C) Arranging blood donation camps and medical check-up camps
(D) Being profitable enough to provide returns to shareholders

Ans :

(C) Arranging blood donation camps and medical check-up camps
The text provides several examples of social responsibility. Arranging blood donation camps, cataract surgery camps, and medical check-ups are listed as examples of philanthropic responsibility. This category involves actively contributing to the welfare of the community through donations of time, services, or money, separate from the core business operations.

Oct/Nov 2005

110. A financial manager is evaluating two investment options. Option A is highly marketable and can be converted to cash within a day but offers a low return. Option B offers a much higher return but may take months to sell. The manager's dilemma is best described by the principle of:
(A) Liquidity and Return
(B) Risk and Return
(C) Opportunity Cost
(D) Diversification

Ans :

(A) Liquidity and Return
This scenario perfectly illustrates the trade-off between liquidity and return. Option A has high liquidity (marketability) but a low return. Option B has low liquidity but a high return. The text explains that an investor often has to strike a balance between the ease of converting an investment to cash and the desired return.

May/June 2020

111. What is the key difference between an Association of Persons (AOP) and a Body of Individuals (BOI) as per the text?
(A) An AOP cannot earn income, whereas a BOI is formed to earn income
(B) A BOI can have companies as members, but an AOP can only have individuals
(C) An AOP is always a registered legal entity, while a BOI is not
(D) An AOP can have both natural and artificial persons as members, while a BOI can only

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have natural persons

Ans :

(D) An AOP can have both natural and artificial persons as members, while a BOI can only have natural persons
The text draws a clear line between the two. It states that members of an AOP can be natural or artificial persons (like companies). In contrast, a BOI is defined as a group of individuals (natural persons) only. This distinction in the type of membership is the primary differentiating factor between them.

Oct/Nov 2015

112. According to the modern approach, the corporate finance function is built on four basic blocks. Which of the following correctly lists three of these four blocks?
(A) Planning, Production, and Marketing
(B) Planning, Decision making, and Controlling
(C) Decision making, Controlling, and Auditing
(D) Organising, Staffing, and Directing

Ans :

(B) Planning, Decision making, and Controlling
The text lists the four basic blocks of the modern corporate finance function as: 1. Planning, 2. Decision making, 3. Organising and Directing, and 4. Controlling. The option "Planning, Decision making, and Controlling" correctly identifies three of these four fundamental building blocks.

May/June 2013

113. A company decides to benefit its shareholders by purchasing its own shares from the open market, thereby reducing the number of outstanding shares. This action is known as:
(A) A dividend payment
(B) A rights issue
(C) A buy back of shares
(D) A private placement

Ans :

(C) A buy back of shares
The text mentions that instead of paying a dividend, companies sometimes decide to benefit shareholders through a buy back of shares. This process involves the company using its cash to repurchase its own stock, which can increase the earnings per share and market value for the remaining shareholders.

Oct/Nov 2021

114. Which of the following is NOT a primary objective of financial management?
(A) To ensure optimum utilization of funds
(B) To decide on optimum capital structure
(C) To determine the day-to-day production schedule
(D) To ensure an appropriate financial risk-management system

Ans :

(C) To determine the day-to-day production schedule
The objectives of financial management include ensuring optimum fund use, deciding capital structure, and managing risk. Determining the daily production schedule is an operational management function. While it has financial implications, the scheduling itself is not a primary objective of the financial management department.

May/June 2024

115. The Indian Partnership Act, 1932, defines partnership but does not specify the maximum number of partners. Which legislation provides this limit?
(A) The Companies Act, 2013 and associated rules
(B) The Limited Liability Partnership Act, 2008
(C) The Income-Tax Act, 1961
(D) The SEBI Act, 1992

Ans :

(A) The Companies Act, 2013 and associated rules
The text clearly states that while the Partnership Act is silent on the maximum number of partners, the limit is imposed by other legislation. It specifies that "as per the Companies Act 2013 and The Companies (Miscellaneous) Rules, 2014, a partnership can have a maximum of 50 persons."

Oct/Nov 2008

116. In the context of the emerging role of a finance manager in India, what has made raising debt for long-term infrastructure projects more difficult?
(A) The abolition of the Capital Issues (Control) Act
(B) The disappearance of Development Financial Institutions (DFIs) and asset-liability mismatch issues for banks
(C) The mandatory 2% CSR spending rule

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CHAPTER 20
Ratio Analysis

May/June 2016

1. What is the primary function of an accounting ratio in financial analysis?

(A) To present standalone absolute figures, such as total sales or net profit, for evaluation.

(B) To benchmark a firm's financial position and performance.

(C) To completely replace the need for detailed financial statements like the balance sheet and income statement.

(D) To quantify non-financial business aspects, such as employee morale or management effectiveness.

Ans :

(B) To benchmark a firm's financial position and performance.

An accounting ratio expresses a mathematical relationship between connected accounting figures. In financial analysis, this ratio acts as a standard or benchmark. It is used to evaluate a firm's financial standing and operational performance, providing meaningful context that absolute figures alone cannot offer, thus enabling more informed judgments about the business.

Oct/Nov 2009

2. According to the text, why are absolute accounting figures considered unfit for comparison on their own?

(A) They lack context and are not meaningful for performance evaluation unless related to other figures.

(B) They involve complex calculations and terminology that are beyond an average investor's comprehension.

(C) They are consistently presented in a deliberately misleading format designed to conceal vital business facts.

(D) They are inherently unstable and subject to frequent revisions due to ongoing price level adjustments.

Ans :

(A) They lack context and are not meaningful for performance evaluation unless related to other figures.

Absolute figures, such as a net profit of Rs. 10 crore, lack context. Their significance can only be judged when they are related to other relevant data, like the firm's sales or investments. Ratios provide this relational context, making them suitable for comparison and analysis, which absolute numbers by themselves cannot achieve.

May/June 2023

3. What condition must be met for a comparison between two sets of figures to be purposeful in ratio analysis?

(A) The figures must be from two different companies operating within the same industry.

(B) The figures must have been audited and certified by the same independent accounting firm.

(C) The figures must be connected with each other in some manner.

(D) The figures must both be positive integers greater than zero and expressed in the same currency.

Ans :

(C) The figures must be connected with each other in some manner.

The fundamental principle of ratio analysis is that the figures being compared must have a logical relationship. Comparing two entirely unconnected figures would not serve any analytical purpose. For instance, comparing a company's sales to its number of employees has a logical basis, whereas comparing its sales to the number of directors' cars does not.

Oct/Nov 2018

4. Which of the following best defines an accounting ratio?

(A) A single-page summary of a company's complete set of financial statements.

(B) An individual, standalone accounting figure,

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(C) I, II, and III
(D) II and III only

Ans :

(D) II and III only
Statement I is incorrect; the text distinguishes co-operatives by their main objectives of "mutual assistance and service," contrasting them with the profit-making aim of other organizations. Statements II and III are correct, as the text confirms that a registered society is a separate legal entity whose management is elected by its members.

Oct/Nov 2012

122. Match the term in List-I with the most appropriate description in List-II.
List-I (Term)
P. Karta
Q. Co-parceners
R. Agent
S. Principal
List-II (Description)
1. The owners of a company (shareholders) in an agency relationship.
2. The senior-most male member who manages an HUF.
3. The members of an undivided Hindu family who own the firm.
4. The managers of a company in an agency relationship.

Code:
(A) P-2, Q-3, R-4, S-1
(B) P-1, Q-2, R-3, S-4
(C) P-2, Q-4, R-3, S-1
(D) P-3, Q-2, R-1, S-4

Ans :

(A) P-2, Q-3, R-4, S-1
The Karta is the senior-most male member managing the HUF (P-2). Co-parceners are the members of the HUF who own it (Q-3). In the shareholder-manager agency relationship, the managers are the agents (R-4), and the shareholders are the principals (S-1).

May/June 2011

123. **Assertion (A) :** Finance may be considered a branch of economics.
Reason (R) : Both finance and economics deal with similar topics like interest rates and marginal cost, but finance has a narrower, more practical focus on managing funds for a specific organisation.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
The text suggests finance can be seen as a branch of economics because they share common ground. The reason correctly elaborates on this relationship, explaining that while they cover similar topics, finance applies economic principles in a narrower, more practical context focused on a single firm's objectives, which justifies its position as a specialized branch.

Oct/Nov 2020

124. Which of the following is NOT an example of a financial decision in a firm?
(A) Deciding to raise Rs. 50 crore through a public issue of equity
(B) Deciding to replace an old machine with a new, more efficient one
(C) Deciding to implement a new performance appraisal system for employees
(D) Deciding to distribute 30% of profits as dividends and retain the rest

Ans :

(C) Deciding to implement a new performance appraisal system for employees
Raising capital, replacing assets (capital budgeting), and deciding dividend policy are all core financial decisions. Implementing a performance appraisal system, while having financial implications, is fundamentally a human resource management decision concerned with employee evaluation, motivation, and development.

May/June 2022

125. Which financial principle is best captured by the idiom, "never put all your eggs in one basket"?
(A) Diversification
(B) The Time Value of Money
(C) The Risk-Return Trade-off
(D) Hedging

Ans :

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norms

Ans :

(A) The relaxation in industrial licensing leading to increased competition
The case directly reflects a challenge discussed in the text regarding the emerging role of the finance manager in India. The relaxation of industrial licensing, a key part of liberalization, led to a surge in competition. This makes the "Selection of project" more challenging, as the finance manager must now evaluate projects in a much more competitive environment.

Oct/Nov 2022

98. A company's finance team decides to rely on an external law firm for all tax-related advisory and compliance matters, allowing the internal team to focus entirely on strategic financial planning and M&A activities. This decision is an example of addressing which question when structuring a finance team?
(A) Do we have the required expert support available internally or do we have to take external support?
(B) What are the fundamental requirements of the finance team?
(C) What are the tools required to simplify and standardise core tasks?
(D) Do team members have an inclination to collaborate with the wider business?

Ans :

(A) Do we have the required expert support available internally or do we have to take external support?
The case shows the team making a strategic choice about sourcing expertise. By outsourcing tax matters, they are acknowledging a potential gap in internal specialist capabilities (or making a strategic choice to use external experts) and freeing up internal resources for other core functions. This directly answers the question of internal versus external support.

May/June 2018

99. Which of the following is NOT a characteristic of a partnership firm as per the Indian Partnership Act, 1932?
(A) It is an association of two or more persons
(B) There is an agreement to carry on a business for sharing profits
(C) The liability of each partner is limited to their capital contribution
(D) The business can be carried on by all or any of them acting for all

Ans :

(C) The liability of each partner is limited to their capital contribution
The text explicitly states that in a partnership firm, unlike a Limited Liability Company (LLC) or LLP, the liability of each partner is unlimited. This means their personal assets can be used to settle the firm's debts. Limited liability is a feature of LLPs and companies, not traditional partnerships.

Oct/Nov 2016

100. A company is considering a project. The risk-free rate of return is 5%. Due to the project's specific uncertainties, the finance manager adds a risk premium of 8%. What would be the Required Rate of Return for this project?
(A) 13%
(B) 3%
(C) 5%
(D) 8%

Ans :

(A) 13%
The Required Rate of Return is calculated using the formula: Required Rate of Return = Risk-free Return + Risk Premium. In this case, it would be 5% + 8% = 13%. This is the minimum return the company should expect from the project to compensate for both the time value of money and the project's specific risk.

May/June 2014

101. An organisation's code of conduct emphasizes principles like Honesty, Integrity, Fairness, and Respect for Others. These principles primarily fall under the domain of:
(A) Financial Engineering
(B) Capital Budgeting
(C) Market Analysis
(D) Business Ethics

Ans :

(D) Business Ethics
The principles listed—Honesty, Integrity, Fairness, and Respect for Others—are fundamental moral and ethical values. When applied in a business context and documented in a code of conduct, they form the core of business

NODIA

(C) II and III only
(D) I, II, and III

Ans :

(A) I and II only
Statement I correctly defines financial management. Statement II is also correct, as the text warns that changing the business form may attract tax liability. Statement III is incorrect; a traditional partnership firm does not have a separate legal status apart from its partners, unlike an LLP or a company.

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(D) The relaxation in industrial licensing requirements

Ans :

(B) The disappearance of Development Financial Institutions (DFIs) and asset-liability mismatch issues for banks
The text highlights that the disappearance of DFIs, which were specialist long-term lenders, created a void. Commercial banks, which stepped in, face an asset-liability mismatch when they use their typically short-term deposits to fund long-duration infrastructure loans, making it more challenging to raise such debt.

May/June 2006

117. A manager of a company is also a 'principal' in a different context. In which of the following agency problem types is the manager acting as a principal?
(A) Shareholders vs. management
(B) Board of directors vs. management
(C) Management vs. employees
(D) The company vs. its suppliers

Ans :

(C) Management vs. employees
While a manager is an agent to the shareholders, they act as a principal in their relationship with the employees who report to them. The employees are agents expected to act in the best interests of the management (and by extension, the company). This creates another layer of principal-agent relationships within the firm.

Oct/Nov 2017

118. Which of the following is NOT listed as a principle of a code of conduct/ethics in business?
(A) Maximizing Short-Term Gains
(B) Corporate Transparency
(C) Customer Prioritisation
(D) Whistle-blower Protection

Ans :

(A) Maximizing Short-Term Gains
The list of principles for a code of conduct includes concepts like transparency, customer focus, and whistle-blower protection, which all promote long-term trust and sustainability. Maximizing short-term gains, especially at the expense of ethical conduct or long-term value, is contrary to the spirit of business ethics.

NODIA

May/June 2008

119. What is the key advantage of inorganic growth through mergers and acquisitions?
(A) It is always less expensive than organic growth and internal expansion
(B) It does not require any significant financial investment or due diligence
(C) It has the benefit of time-saving compared to creating fresh capacity
(D) It is a completely risk-free method of achieving business expansion

Ans :

(C) It has the benefit of time-saving compared to creating fresh capacity
The text points out that creating fresh capacity (organic growth) is a time-consuming process. Inorganic growth through mergers and acquisitions offers a significant advantage in terms of speed. A company can quickly gain capacity, market share, or technology by acquiring an existing firm, saving valuable time.

Oct/Nov 2013

120. A financial decision based on "scant and unconfirmed data" is more likely to:
(A) Go wrong in its purpose
(B) Succeed in its purpose
(C) Be perfectly accurate
(D) Be praised by auditors

Ans :

(A) Go wrong in its purpose
The text emphasizes the importance of a solid data foundation for financial decisions. It explicitly states, "A financial decision based on scant and unconfirmed data is more likely to go wrong in its purpose." This underscores the critical link between the quality of accounting data and the quality of financial management decisions.

May/June 2015

121. Consider the following statements regarding a Co-operative society:
I. Its main objective is profit making, similar to a company.
II. A registered co-operative society is recognized as a separate legal entity.
III. Its management is vested in a committee elected by its members.
Which of the above statements are correct?
(A) I and II only
(B) I and III only

such as total revenue, reported on a financial statement.
(C) A formal, guaranteed forecast of a company's future profitability, solvency, and stock price.
(D) A mathematical relationship between logically connected accounting figures.

Ans :

(D) A mathematical relationship between logically connected accounting figures.
An accounting ratio is a mathematical expression that quantifies the relationship between two or more accounting figures that are logically connected. This expression can be a percentage, a proportion, or a fraction. The purpose is to derive meaningful insights that are not apparent from examining the absolute figures in isolation from each other.

May/June 2007

5. Under the traditional classification, ratios calculated using figures solely from the balance sheet are known as what?
(A) Profit and loss account ratios
(B) Composite ratios
(C) Balance sheet ratios
(D) Inter-statement ratios

Ans :

(C) Balance sheet ratios
The traditional classification system categorizes ratios based on the financial statement from which their components are derived. Ratios that are calculated exclusively using figures found within the balance sheet, such as the current ratio or debt-equity ratio, are referred to as balance sheet ratios under this classification method, focusing on the firm's financial position.

Oct/Nov 2025

6. What is another name for composite ratios in the traditional classification system?
(A) Balance sheet ratios
(B) Inter-statement ratios
(C) Profitability ratios
(D) Solvency ratios

Ans :

(B) Inter-statement ratios
Under the traditional classification, composite ratios are also known as inter-statement ratios. This name is appropriate because they are calculated using figures from both the profit and loss account and the balance sheet. This combines performance data with financial position data, such as the Return on Capital Employed, which links profit to assets.

May/June 2012

7. Which category of ratios, under the traditional classification, is calculated using figures from both the profit and loss account and the balance sheet?
(A) Profit and loss account ratios
(B) Balance sheet ratios
(C) Liquidity ratios
(D) Composite ratios

Ans :

(D) Composite ratios
Composite ratios, also called inter-statement ratios, are derived from figures that originate from two different financial statements. Specifically, they combine data from the profit and loss account (an income statement item) with data from the balance sheet (a position statement item) to provide a more holistic view of the company's performance and efficiency.

Oct/Nov 2014

8. Why is the traditional classification of ratios considered "too crude and unsuitable" for modern financial analysis?
(A) It fails to recognize that the balance sheet and income statement must be studied together.
(B) It includes too many complex formulas that are difficult for analysts to calculate manually.
(C) It focuses exclusively on short-term financial health while ignoring long-term solvency.
(D) It was designed for manufacturing industries and is not applicable to modern service sectors.

Ans :

(A) It fails to recognize that the balance sheet and income statement must be studied together.
The traditional classification is deemed unsuitable because it encourages analyzing the balance sheet and income statement in isolation. Modern financial analysis emphasizes that these statements are interdependent. A comprehensive understanding of a business's profitability and solvency requires studying them together, which the functional classification system facilitates more effectively than the traditional one.

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are being implemented in a phased manner to replace the existing accounting standards issued by the ICAI.

Oct/Nov 2005

26. Which of the following statements is incorrect regarding the limitations of accounting ratios?

(A) Ratios are only indicators and cannot be taken as final proof of a firm's financial position.

(B) A high current ratio always means the company has a good liquid position.

(C) The practice of "window dressing" can make ratios misleading.

(D) The effects of price level changes can distort financial analysis based on ratios.

Ans :

(B) A high current ratio always means the company has a good liquid position.

This statement is incorrect. The text explicitly states that a high current ratio does not necessarily mean a good liquid position, especially if the current assets consist mostly of outdated or slow-moving stocks. Ratios are merely indicators that signal the need for further investigation; they are not conclusive proof on their own.

May/June 2020

27. What does the observation "Ratios may be likened to railroads. They tell the analyst 'stop, look and listen'" imply?

(A) Ratios are an outdated tool of financial analysis, much like railroads in the modern era.

(B) Ratios provide a clear and direct path to making profitable investment decisions.

(C) Ratios are a specialized tool primarily useful for companies in the transportation industry.

(D) Ratios are warning signals that require further investigation, not definitive conclusions.

Ans :

(D) Ratios are warning signals that require further investigation, not definitive conclusions.

This analogy suggests that ratios serve as indicators or warning signals, much like the signs at a railroad crossing. They alert the analyst to potential strengths or weaknesses ("stop"), prompt a deeper examination of the underlying facts ("look"), and require careful consideration of all relevant factors before a judgment is made ("listen").

Oct/Nov 2015

28. What is "Window Dressing" in the context of accounting?

(A) The manipulation of accounts to conceal vital facts and present a better-than-actual position.

(B) The process of making financial statements aesthetically pleasing with graphs and charts.

(C) The legally required adjustment of accounts to reflect inflation and other price level changes.

(D) The common practice of decorating a company's office before an important analyst meeting.

Ans :

(A) The manipulation of accounts to conceal vital facts and present a better-than-actual position.

Window dressing refers to the manipulation of financial accounts to hide unfavorable information and present a more favorable financial position than what is real. This can involve actions taken to artificially improve certain ratios just before the reporting date, making the company appear healthier or more efficient than it actually is.

May/June 2013

29. A company has current assets of ₹4,000 and current liabilities of ₹2,000. To improve its current ratio before the balance sheet date, which action could the management take?

(A) Purchase goods worth ₹2,000 on credit.

(B) Take a short-term loan of ₹1,000.

(C) Pay off current liabilities of ₹1,000.

(D) Declare a dividend of ₹1,000 to be paid next month.

Ans :

(C) Pay off current liabilities of ₹1,000.

Initially, the current ratio is

$$\frac{4,000}{2,000} = 2$$

By paying off ₹1,000 of current liabilities, current assets become ₹3,000 and current liabilities become ₹1,000. The new current ratio is 3. This action, a form of window dressing, improves the ratio. Purchasing goods on credit would reduce the ratio to 1.5.

Oct/Nov 2021

30. A company's management wants to show a high stock turnover ratio to appear operationally

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Ratios (Functional) correctly matches a category from each system.

Oct/Nov 2022

14. How do accounting ratios "simplify financial statements"?

(A) By replacing complex financial statements with a single, easy-to-understand number.
(B) By eliminating the need for users to read the detailed notes accompanying the accounts.
(C) By converting all financial data from numerical format into a standardized graphical format.
(D) By summarizing the narrative of changes in the financial condition of the business.

Ans :

(D) By summarizing the narrative of changes in the financial condition of the business.
Ratios simplify the comprehension of financial statements by distilling large amounts of data into a few key indicators. They help to tell the story of a company's financial journey and condition in a more digestible format. Instead of analyzing raw numbers, users can look at trends and relationships, making complex financial information easier to understand.

May/June 2018

15. What is the primary benefit of using ratios for inter-firm comparison?

(A) It highlights factors associated with success and failure, revealing strong and weak firms.
(B) It guarantees that the compared firms have identical accounting policies and business models.
(C) It provides a definitive ranking of firms from best to worst without requiring further analysis.
(D) It focuses solely on comparing the profitability of different companies while ignoring their solvency.

Ans :

(A) It highlights factors associated with success and failure, revealing strong and weak firms.
Inter-firm comparison using ratios allows an analyst to benchmark a company against its competitors or the industry average. This process helps to identify the characteristics that distinguish successful firms from unsuccessful ones. By doing so, it can reveal which firms are strong, weak, overvalued, or undervalued relative to their peers in the market.

Oct/Nov 2016

16. What purpose does intra-firm comparison of ratios serve?

(A) To compare the company's performance with its main competitors in the same industry.
(B) To evaluate the efficiency of different divisions or business units within the same firm.
(C) To ensure the firm's compliance with international accounting standards and local tax laws.
(D) To determine the precise market value of the company's shares for potential investors.

Ans :

(B) To evaluate the efficiency of different divisions or business units within the same firm.
Intra-firm comparison involves comparing the performance of different departments, divisions, or business units within the same organization. This use of ratios helps management assess the relative efficiency of these internal segments. It can highlight areas of strength and weakness, aiding in decisions about resource allocation and future operational strategies within the firm.

May/June 2014

17. How do accounting ratios assist in the management function of planning and forecasting?

(A) By providing exact, non-negotiable predictions of future sales volumes and net profits.
(B) By establishing historical norms that can indicate future trends, successes, or problems.
(C) By automatically adjusting all historical financial data for inflation and other price level changes.
(D) By replacing the need for managerial judgment, intuition, and complex decision-making processes.

Ans :

(B) By establishing historical norms that can indicate future trends, successes, or problems.
Over time, a firm or industry develops certain ratio norms. By tracking these ratios, management can identify significant changes or trends in the firm's data. These trends can provide valuable clues about future opportunities or potential problems,

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thereby assisting management in its basic functions of forecasting, planning, coordination, control, and communication.

Oct/Nov 2007

18. Which of the following is NOT listed as a primary use of accounting ratios?
(A) To determine the final, legal valuation of a business.
(B) To simplify complex financial statements.
(C) To facilitate inter-firm and intra-firm comparison.
(D) To help in corporate planning and forecasting.

Ans :

(A) To determine the final, legal valuation of a business.
The text describes the uses of ratios as simplifying statements, enabling inter-firm and intra-firm comparisons, and aiding in planning and forecasting. Ratios are analytical tools, not valuation mechanisms. While they contribute to the information used in a business valuation, they do not, by themselves, determine the final or legal value of an enterprise.

May/June 2025

19. What is a key requirement for ratios to be useful in judging the efficiency of a business?
(A) They must be calculated and certified by an independent third-party auditing firm.
(B) They must be presented in a standardized graphical format for easy interpretation.
(C) They must be compared with past results or results of a similar business for context.
(D) They must focus exclusively on profitability metrics to assess overall business efficiency.

Ans :

(C) They must be compared with past results or results of a similar business for context.
A ratio in isolation has limited value. Its utility in judging business efficiency comes from comparison. By comparing current ratios with the company's own historical ratios (trend analysis) or with the ratios of similar businesses (industry analysis), an analyst can identify performance trends and relative strengths or weaknesses, providing a context for judgment.

Oct/Nov 2019

20. Why might a forecast based on past ratio performance not prove correct for the future?
(A) Because other factors like market conditions and management policies can affect future operations.
(B) Because accounting principles strictly prohibit the use of any historical data for forecasting.
(C) Because financial ratios are static figures that are specifically designed not to change over time.
(D) Because financial statements are inherently inaccurate and thus unreliable for any future predictions.

Ans :

(A) Because other factors like market conditions and management policies can affect future operations.
While historical ratio analysis provides a glimpse into past performance, it is not a perfect predictor of the future. The business environment is dynamic, and various external and internal factors, such as changing market conditions, competitive pressures, new regulations, or shifts in management policies, can significantly impact future operations, making historical trends an unreliable sole guide.

May/June 2009

21. A significant limitation of accounting ratios is that they are based only on information recorded in financial statements. What type of important information is consequently ignored?
(A) Historical profit figures and past performance trend data.
(B) The company's total outstanding debt and other liabilities.
(C) The total amount of cash and cash equivalents held by the company.
(D) Non-financial factors like a change in management or employee morale.

Ans :

(D) Non-financial factors like a change in management or employee morale.
Ratios are derived from financial statements, which primarily capture quantifiable monetary transactions. Consequently, they are subject to the same limitations as these statements. Important non-financial factors, such as the quality of the management team, employee morale, or a recent change in key leadership, are not reflected in

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ratios but can have a profound effect on future profitability.

Oct/Nov 2011

22. Why can the comparison of ratios between two firms be misleading if their accounting policies differ?

(A) Because using different accounting policies is an illegal practice that results in regulatory penalties.

(B) Variations in policies for inventory, depreciation, or R&D affect the underlying reported figures.

(C) Because if policies differ, it strongly implies that one of the firms is engaging in fraudulent reporting.

(D) Because ratios are only designed to be comparable if the firms operate in completely different industries.

Ans :

(B) Variations in policies for inventory, depreciation, or R&D affect the underlying reported figures.

Management has discretion in choosing accounting policies for areas like inventory valuation (e.g., FIFO vs. LIFO), depreciation methods, and the treatment of R&D costs. Different choices lead to different reported figures for profits and assets. Comparing ratios of two firms without adjusting for these policy differences can be misleading and meaningless, as the comparison is not on a like-for-like basis.

May/June 2010

23. What action must a financial analyst take before undertaking a financial analysis using ratios?

(A) Assume all companies being analyzed use identical accounting policies without verification.

(B) Ignore all non-financial information about the companies, as it is irrelevant to ratio analysis.

(C) Carefully examine financial statements and make adjustments based on disclosed accounting policies.

(D) Recalculate all financial statements from scratch using a single, personally preferred accounting method.

Ans :

(C) Carefully examine financial statements and make adjustments based on disclosed accounting policies.

Given that companies can use different accounting policies and may even change their own policies over time, a financial analyst cannot take the figures at face value. It is absolutely necessary to conduct a close scrutiny of the financial statements and their accompanying disclosures. The analyst must make appropriate adjustments to ensure comparability before attempting any meaningful analysis with ratios.

Oct/Nov 2024

24. What international body is mentioned as having been established to promote the standardization of accounting policies?

(A) The Ministry of Corporate Affairs (MCA)

(B) The Institute of Chartered Accountants of India (ICAI)

(C) The World Trade Organization (WTO)

(D) The International Accounting Standards Board (IASB)

Ans :

(D) The International Accounting Standards Board (IASB)

The text states that a growing realization for the need to standardize accounting policies led to the establishment of the International Accounting Standards Board (IASB). This body is responsible for issuing International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) to create a common global language for business affairs.

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May/June 2017

25. In India, which authority has issued the Indian Accounting Standards (Ind AS) that are converged from IFRS?

(A) The Ministry of Corporate Affairs (MCA)

(B) The Reserve Bank of India (RBI)

(C) The Securities and Exchange Board of India (SEBI)

(D) The Supreme Court of India

Ans :

(A) The Ministry of Corporate Affairs (MCA)

The chapter specifies that in India, the Indian Accounting Standards (Ind AS), which are converged from the International Financial Reporting Standards (IFRS), have been issued by the Ministry of Corporate Affairs. These standards

May/June 2019

9. Which of the following is NOT one of the categories under the functional classification of ratios?
(A) Profitability Ratios
(B) Turnover or activity ratios
(C) Composite Ratios
(D) Financial or solvency ratios

Ans :

(C) Composite Ratios
The functional classification groups ratios based on the analytical purpose they serve. The main categories are Profitability Ratios, Turnover or Activity Ratios, and Financial or Solvency Ratios. 'Composite Ratios' is a category from the older, traditional classification system, which is based on the source of data rather than its analytical function.

Oct/Nov 2006

10. Financial or solvency ratios are further subdivided into which two categories?
(A) Short-term Solvency Ratios and Long-term Solvency Ratios
(B) Overall Profitability and Specific Profitability Ratios
(C) Internal Performance Ratios and External Benchmark Ratios
(D) Primary Liquidity Ratios and Secondary Activity Ratios

Ans :

(A) Short-term Solvency Ratios and Long-term Solvency Ratios
Financial ratios, which assess a firm's solvency, are divided into two sub-categories based on the time horizon. Short-term solvency ratios evaluate the firm's ability to meet its immediate obligations, while long-term solvency ratios assess its financial stability and ability to meet its obligations over a longer period. This distinction is crucial for creditors and investors.

May/June 2021

11. What is the alternative term used by some accountants for Short-term Solvency Ratios?
(A) Gearing Ratios
(B) Activity Ratios
(C) Profitability Ratios
(D) Liquidity Ratios

Ans :

(D) Liquidity Ratios
Short-term solvency ratios are designed to disclose the financial position and solvency of a firm in the short period. Because they measure the firm's ability to convert assets into cash to meet current obligations, some accountants prefer to call them 'Liquidity Ratios'. This term emphasizes the focus on the liquid state of the company's assets.

Oct/Nov 2010

12. What is the simpler term some accountants prefer for Long-term Solvency Ratios?
(A) Liquidity Ratios
(B) Solvency Ratios
(C) Capital Structure Ratios
(D) Leverage Ratios

Ans :

(B) Solvency Ratios
Long-term solvency ratios are used to assess the financial position and solvency of a firm over the long run. While the full name is descriptive, some accountants simplify this by referring to them merely as 'Solvency Ratios'. This is because long-term financial health is often seen as the core definition of solvency for a business.

May/June 2005

13. Which of the following statements correctly identifies a pair of ratio classifications?
(A) Traditional Classification: Profitability Ratios; Functional Classification: Balance Sheet Ratios
(B) Traditional Classification: Activity Ratios; Functional Classification: Inter-statement Ratios
(C) Traditional Classification: Composite Ratios; Functional Classification: Turnover Ratios
(D) Traditional Classification: Liquidity Ratios; Functional Classification: Solvency Ratios

Ans :

(C) Traditional Classification: Composite Ratios; Functional Classification: Turnover Ratios
The text outlines two main classification systems. The traditional system includes categories like Profit and Loss Account Ratios, Balance Sheet Ratios, and Composite Ratios. The functional system includes categories like Profitability Ratios, Turnover or Activity Ratios, and Financial or Solvency Ratios. The pairing of Composite Ratios (Traditional) and Turnover

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efficient. According to the text, how might this be deceptively achieved?

(A) By making unwarranted price reductions to boost sales volume.
(B) By significantly increasing the selling price of all goods sold.
(C) By holding a large and excessive stock of inventory at the year-end.
(D) By revaluing the existing stock at a much higher cost basis.

Ans :

(A) By making unwarranted price reductions to boost sales volume.
The text explains that a high stock turnover ratio, generally a sign of efficiency, could be achieved through dubious means. One such method is implementing unwarranted price reductions. This can artificially inflate sales volume and thus the turnover ratio, but it may harm profitability and does not reflect true operational efficiency.

May/June 2024

31. Why does financial analysis based on traditional accounting ratios give misleading results when price level changes are not considered?

(A) Because profits are always artificially overstated during periods of high inflation.
(B) Because all companies are required by international law to adjust their statements for inflation.
(C) Because liabilities are completely unaffected by any price level changes over time.
(D) Because it's difficult to compare firms set up in different years with assets of different ages.

Ans :

(D) Because it's difficult to compare firms set up in different years with assets of different ages.
When price levels change significantly over time, historical cost accounting can distort comparisons. For example, an older company's assets are recorded at a much lower cost than a newer company's assets. Consequently, the depreciation charge for the older company will be lower, artificially inflating its profit figures compared to the newer company.

Oct/Nov 2008

32. Which accounting techniques are mentioned as being helpful in addressing the problems of price level changes?

(A) First-In, First-Out (FIFO) and Last-In, First-Out (LIFO)
(B) Current purchasing power and current cost accounting
(C) Double-entry bookkeeping and accrual accounting
(D) Ratio analysis and trend analysis

Ans :

(B) Current purchasing power and current cost accounting
To counter the distortions caused by price level changes in historical cost accounting, the text suggests that financial statements should be adjusted. The techniques mentioned as being quite helpful in this respect are current purchasing power (CPP) accounting and current cost accounting (CCA), which aim to present financial information in terms of current values.

May/June 2006

33. What is the limitation of ratio analysis regarding "fixed standards"?

(A) The standards for ideal ratios are legally fixed by regulators and cannot be changed.
(B) The standards for ratios are fixed by the IASB and must be universally applied by all firms.
(C) No fixed standards can be laid down for ideal ratios, as context and industry norms matter.
(D) Each company must fix its own standards for ratios and never deviate from them year to year.

Ans :

(C) No fixed standards can be laid down for ideal ratios, as context and industry norms matter.
The text argues that no universal, fixed standards exist for what constitutes an "ideal" ratio. For example, while a current ratio of 2 is often cited as ideal, a firm with strong banking relationships might operate perfectly well with a ratio of 1. The appropriate benchmark depends on the industry, company size, and specific circumstances.

Oct/Nov 2017

34. The conclusion states that ratio analysis, if done mechanically, is "not only misleading but also dangerous." What does this imply?

(A) Ratio analysis should always be automated using software to avoid any human error.
(B) The calculations involved in ratio analysis are inherently complex and prone to dangerous errors.

NODIA

(C) Ratio analysis is an outdated technique that should be avoided by modern management.
(D) It requires understanding and sensitive judgment rather than just mechanical calculation.

Ans :

(D) It requires understanding and sensitive judgment rather than just mechanical calculation. The text describes ratio analysis as a "double-edged sword." It is a useful aid for decision-making when ratios are calculated discriminately and interpreted wisely. However, if used as a mechanical substitute for thinking and judgment, it becomes worse than useless, leading to misleading and potentially dangerous conclusions about the business's health.

May/June 2008

35. What is the formula for calculating the Overall Profitability Ratio, also known as Return on Investment (ROI)?
(A) $\frac{\text{Net Profit}}{\text{Capital Employed}} \times 100$
(B) $\frac{\text{Operating Profit}}{\text{Total Sales}} \times 100$
(C) $\frac{\text{Operating Profit}}{\text{Capital Employed}} \times 100$
(D) $\frac{\text{Gross Profit}}{\text{Capital Employed}} \times 100$

Ans :

(C) $\frac{\text{Operating Profit}}{\text{Capital Employed}} \times 100$

The Overall Profitability Ratio, or Return on Investment (ROI), is designed to indicate the percentage of return generated on the total capital employed in the business. It is calculated by dividing the operating profit by the capital employed and multiplying the result by 100 to express it as a percentage.

Oct/Nov 2013

36. Which of the following is NOT listed as a popular meaning for the term 'capital employed'?
(A) The sum total of all assets, whether they are fixed or current.
(B) The sum total of all fixed assets shown on the balance sheet.
(C) The sum total of current assets minus current liabilities.
(D) The sum total of long-term funds employed in the business operations.

Ans :

(C) The sum total of current assets minus current liabilities.
The text provides three popular meanings for 'capital employed': (i) the sum of all assets, (ii) the sum of fixed assets, and (iii) the sum of long-term funds (Share capital + Reserves + Long-term loans - Non-business/fictitious assets). 'Current assets minus current liabilities' defines working capital, which is not listed as a definition for capital employed.

May/June 2015

37. In management accounting, what is the generally accepted definition of 'capital employed' for calculating ROI?
(A) The sum total of all assets, including both fixed and current categories.
(B) The sum total of fixed assets only, excluding any current or intangible assets.
(C) The total equity of the firm, including preference capital, equity capital, and all reserves.
(D) Share capital + Reserves and surplus + Long-term loans – [Non-business assets + fictitious assets].

Ans :

(D) Share capital + Reserves and surplus + Long-term loans – [Non-business assets + fictitious assets].
While there are different interpretations, the text specifies that in management accounting, 'capital employed' is generally understood to mean the total long-term funds invested in the business. This is calculated as the sum of share capital, reserves, and long-term loans, from which any non-business and fictitious assets are deducted to reflect true operational capital.

Oct/Nov 2012

38. How is 'Operating Profit' defined for the purpose of calculating ROI?
(A) Profit before interest and tax.
(B) Profit after interest and tax.
(C) Gross profit minus all administrative expenses.
(D) Net profit as shown in the Profit and Loss Account.

Ans :

(A) Profit before interest and tax.
For the calculation of Return on Investment (ROI), 'Operating Profit' is defined as profit

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before deducting interest and tax (PBIT). The 'interest' component specifically refers to interest on long-term borrowings. This measure reflects the profit generated from the core operations of the business before considering financing costs and taxes.

May/June 2011

39. When computing operating profit for ROI, which of the following items should be excluded?
(A) Depreciation on factory machinery.
(B) Salaries of administrative staff.
(C) Interest income on Government securities.
(D) Cost of goods sold.

Ans :

(C) Interest income on Government securities.
Operating profit is meant to reflect earnings from a company's primary business activities. Therefore, non-trading incomes, such as interest earned on investments like Government securities, and non-trading losses or expenses, like loss from a fire, are excluded from its calculation. These items are not related to the core operational performance of the business.

Oct/Nov 2020

40. What is another term used to express the concept of Return on Investment (ROI)?
(A) Yield on Capital
(B) Earnings Per Share
(C) Net Profit Margin
(D) Dividend Payout Ratio

Ans :

(A) Yield on Capital
The concept of ROI measures the profit a firm earns on investing a unit of capital. The text states that 'Yield on capital' is another term employed to express this same idea. Both terms refer to the efficiency with which a company uses its capital to generate profits from its operations.

May/June 2022

41. What is the primary significance of the Return on Investment (ROI) ratio?
(A) It directly determines the market price of a company's shares on the stock exchange.
(B) It exclusively measures the short-term liquidity position of a firm and its working capital.
(C) It calculates the exact amount of dividend that will be paid to all classes of shareholders.
(D) It is a dependable measure for judging the overall efficiency or inefficiency of a business.

Ans :

(D) It is a dependable measure for judging the overall efficiency or inefficiency of a business.
ROI is a comprehensive measure because profit is the net result of all business operations. By relating this profit to the capital used to generate it, the ratio collectively expresses all efficiencies and inefficiencies of the business. This makes it a reliable tool for judging overall performance and comparing the efficiency of different departments, plants, or companies.

Oct/Nov 2023

42. For the purpose of comparing the efficiency of different departments or companies using ROI, what is considered as 'capital'?
(A) Only the equity share capital provided by the common stockholders.
(B) The aggregate of all capital at the disposal of the company.
(C) Only the long-term debt and debentures issued by the company.
(D) The net working capital, calculated as current assets minus current liabilities.

Ans :

(B) The aggregate of all capital at the disposal of the company.
When using ROI for broad efficiency comparisons, 'capital' is considered to be the total aggregate capital available to the company. This includes all sources of funds, such as equity capital, preference capital, reserves, and debentures. 'Profit' in this context is taken before deductions for interest, income tax, and dividends to reflect the return on total capital.

May/June 2016

43. A company borrows funds at an interest rate of 8 %. Its calculated Return on Investment (ROI) is 7.5%. What does this situation indicate about the company's borrowing policy?
(A) The borrowing was economically wise and highly fruitful for the shareholders.
(B) The company is employing its borrowed funds with maximum efficiency.
(C) It would have been better not to borrow the funds, unless vital for survival.
(D) The company should immediately borrow more funds to improve its overall ROI.

NODIA

Ans :

(C) It would have been better not to borrow the funds, unless vital for survival.

This scenario demonstrates a negative leverage situation where the return generated by the capital (7.5 %) is less than the cost of borrowing that capital (8%). This indicates that the borrowing was not economically wise, as it reduces overall profitability. Unless borrowing was absolutely essential for the company's survival, it was an inefficient use of funds.

Oct/Nov 2009

44. If ROI is calculated on equity shareholders' capital instead of total capital employed, what does the resulting figure indicate?

(A) The overall operational efficiency of the entire business.
(B) The efficiency and wisdom of the company's borrowing policy.
(C) The company's ability to meet its long-term debt obligations.
(D) The maximum rate of dividend that might be declared.

Ans :

(D) The maximum rate of dividend that might be declared.

When ROI is calculated using profit available to equity shareholders (after interest, tax, and preference dividends) and compared against equity shareholders' funds, it no longer measures overall operational efficiency. Instead, it reflects the return available specifically to equity owners, thereby indicating the potential or maximum rate of dividend that could be distributed.

May/June 2023

45. According to the text, what is the fundamental condition for a business to survive?

(A) The return on capital employed must be more than the cost of capital employed.
(B) The company must consistently achieve a high gross profit margin on its products.
(C) The company's share price must show a positive increase every single year.
(D) The company must avoid all forms of borrowing and operate entirely on equity funds.

Ans :

(A) The return on capital employed must be more than the cost of capital employed.

For a business to be viable and survive in the long run, it must generate a return on its investments that exceeds the cost of acquiring those funds. If the return on capital employed (ROI) is consistently lower than the cost of that capital (e.g., interest on debt, expected return for equity), the business is destroying value and is unsustainable.

Oct/Nov 2018

46. Under what condition can ROI give satisfactory results for comparing the profitability of two or more firms?

(A) When the firms are in different industries.
(B) When the firms are of the same age and of the same size.
(C) When one firm is profitable and the other is loss-making.
(D) When the firms use different accounting policies.

Ans :

(B) When the firms are of the same age and of the same size.

ROI can be a problematic measure for comparing firms of different ages and sizes due to issues like historical cost accounting and economies of scale. The text suggests that to mitigate this risk and get satisfactory comparative results, ROI is most effective when the firms being compared are of a similar age and size.

May/June 2007

47. What is the formula for calculating Earnings per Share (EPS)?

(A) $\frac{\text{Net profit before tax}}{\text{Number of equity shares}}$
(B) $\frac{\text{Operating Profit}}{\text{Number of equity shares}}$
(C) $\frac{\text{Net profit after tax and pref.dividend}}{\text{Number of equity shares}}$
(D) $\frac{\text{Net sales}}{\text{Number of equity shares}}$

Ans :

(C) $\frac{\text{Net profit after tax and pref.dividend}}{\text{Number of equity shares}}$

Earnings per Share (EPS) represents the portion of a company's profit allocated to each outstanding share of common stock. It is calculated by taking the net profit remaining after paying taxes and

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preference dividends and dividing it by the total number of equity shares currently issued.

Oct/Nov 2025

48. Which of the following is a key significance of the Earnings per Share (EPS) ratio?
(A) It measures the company's ability to pay its current liabilities on time.
(B) It helps in determining the market price of the equity share.
(C) It indicates the overall efficiency of inventory management.
(D) It shows the proportion of total debt in the capital structure.

Ans :

(B) It helps in determining the market price of the equity share.
The EPS figure is a crucial factor for investors and is closely linked to the market price of a company's equity shares. A higher EPS is generally seen as favorable and can lead to a higher share price. It also helps in comparing the effective use of equity capital and estimating a company's dividend-paying capacity.

May/June 2012

49. What does the Price Earning (P/E) Ratio indicate?
(A) The relationship between the company's total debt and its total equity.
(B) The percentage of net profit earned on each dollar of sales revenue.
(C) The number of times the earning per share is covered by its market price.
(D) The number of times the company's inventory is sold during an accounting period.

Ans :

(C) The number of times the earning per share is covered by its market price.
The P/E ratio is a valuation metric that indicates how many times the market is willing to pay for each rupee of a company's earnings. It is calculated by dividing the market price per equity share by the earning per share, showing the multiple of earnings that the stock is trading at.

Oct/Nov 2014

50. What does the Price-Earnings (P/E) ratio reflect about a company?
(A) The investor's expectations about growth in the firm's earnings.
(B) Its current liquidity position and ability to meet short-term debt.
(C) Its historical dividend payment record over the past decade.
(D) The average age of the company's depreciable fixed assets.

Ans :

(A) The investor's expectations about growth in the firm's earnings.
The P/E ratio is a forward-looking indicator that helps investors decide whether to buy a company's shares at a particular price. A high P/E ratio often suggests that investors have high expectations for the company's future earnings growth, and they are willing to pay a premium for those anticipated future earnings.

May/June 2019

51. What relationship does the Gross Profit Ratio express?
(A) The relationship between gross profit and total assets.
(B) The relationship between gross profit and operating expenses.
(C) The relationship between gross profit and capital employed.
(D) The relationship between gross profit and net sales.

Ans :

(D) The relationship between gross profit and net sales.
The Gross Profit Ratio is a profitability ratio that measures the relationship between a company's gross profit and its net sales. It is calculated by dividing gross profit by net sales and is usually expressed as a percentage. This ratio indicates the basic profitability of the products sold before accounting for other business expenses.

Oct/Nov 2006

52. What is the formula for the Gross Profit Ratio?
(A) $\frac{\text{Net sales}}{\text{Gross profit}} \times 100$
(B) $\frac{\text{Gross profit}}{\text{Net sales}} \times 100$
(C) $\frac{\text{Gross profit}}{\text{Cost of goods sold}} \times 100$
(D) $\frac{\text{Gross profit}}{\text{Operating exp enses}} \times 100$

Ans :

(B) $\frac{\text{Gross profit}}{\text{Net sales}} \times 100$

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credit and collections. It suggests that credit sales are being converted into cash quickly, which is favorable for the company's cash flow.

Oct/Nov 2014

92. What does the Debt Collection Period Ratio measure?

(A) The average number of days a company takes to pay its suppliers and other creditors.
(B) The average debt collection period.
(C) The total amount of credit sales made during a specific accounting year.
(D) The profitability of sales that are made to customers on a credit basis.

Ans :

(B) The average debt collection period.
The Debt Collection Period Ratio calculates the average amount of time, usually in days or months, that it takes for a company to collect the cash from its accounts receivable. It directly measures the average age of the debtors and indicates how long funds are blocked in receivables after a credit sale is made.

May/June 2019

93. Question 93. Which of the following is a valid method for calculating the Debt Collection Period Ratio?

(A) $\frac{\text{Debtors' turn over}}{\text{Months (or days) in a year}}$
(B) Average account receivable $\times$ Credit sales for the year
(C) $\frac{\text{Average accounts receivable} \times \text{Months (or days) in a year}}{\text{Credit sales for the year}}$
(D) $\frac{\text{Credit sales for the year}}{\text{Months (or days) in a year}}$

Ans :

(C) $\frac{\text{Average accounts receivable} \times \text{Months (or days) in a year}}{\text{Credit sales for the year}}$

The text lists three methods for calculation. One of these methods is to take the average accounts receivable, multiply it by the number of months (12) or days (365) in a year, and then divide the result by the total credit sales for that year. This formula directly computes the average collection period.

Oct/Nov 2006

94. What does a shorter Debt Collection Period imply about a company's debtors?

(A) The debtors are of poor quality and are highly likely to default on their payments.
(B) The company has a very lenient and overly liberal credit policy with its customers.
(C) The company is experiencing a significant and worrying decline in its credit sales.
(D) Prompt payment by debtors and a reduced chance of bad debts.

Ans :

(D) Prompt payment by debtors and a reduced chance of bad debts.
A shorter collection period signifies that debtors are paying their bills quickly. This promptness measures the quality of the debtors and the effectiveness of the company's collection efforts. It also reduces the chances of receivables becoming uncollectible (bad debts) and improves the company's cash flow and liquidity position.

May/June 2021

95. A longer collection period implies too liberal and inefficient credit collection performance. What is the risk of having a credit policy that is too restrictive?

(A) It will result in lower sales which will reduce profits.
(B) It will substantially increase the amount of bad debts.
(C) It will lead to an unmanageably high debtors' turnover ratio.
(D) It will cause the company to have a dangerous excess of cash.

Ans :

(A) It will result in lower sales which will reduce profits.
While a liberal credit policy can lead to bad debts, a policy that is too restrictive can also be detrimental. A very tight credit policy may deter potential customers who require credit terms, leading to a loss of sales. This reduction in sales volume will, in turn, reduce the company's overall profits.

Oct/Nov 2010

96. As a general rule, the amount of receivables should not exceed how many months' credit sales?

(A) One to two months
(B) Three to four months
(C) Five to six months
(D) Over six months

Ans :

NODIA

(C) Market conditions, such as a boom or depression period.
(D) The number of employees in the company.

Ans :

(D) The number of employees in the company.
When evaluating the Net Profit Ratio, an investor must consider its context. This includes the company's cost of capital, benchmark returns for the industry, and prevailing economic conditions. The number of employees, while an operational detail, is not a direct external benchmark used to judge the adequacy of the net profit margin itself.

Oct/Nov 2016

58. When is a company considered to be financially sound or solvent?
(A) When its reported profits are increasing every consecutive year.
(B) When it has no long-term debt in its overall capital structure.
(C) When its market share price is currently at an all-time high.
(D) When it can carry on its business and meet all obligations without strain.

Ans :

(D) When it can carry on its business and meet all obligations without strain.
Solvency refers to a company's financial health and its ability to meet its financial obligations, both long-term and short-term, as they fall due. A solvent company can operate its business smoothly without financial strain, indicating a stable and sound financial position capable of sustaining its operations and commitments.

May/June 2014

59. What is the formula for the Fixed Assets Ratio?
(A) $\frac{\text{Long} - \text{term funds}}{\text{Fixed assets}}$
(B) $\frac{\text{Fixed assets}}{\text{Total assets}}$
(C) $\frac{\text{Fixed assets}}{\text{Long} - \text{term funds}}$
(D) $\frac{\text{Fixed assets}}{\text{Share holder's funds}}$

Ans :

(C) $\frac{\text{Fixed assets}}{\text{Long} - \text{term funds}}$
The Fixed Assets Ratio is a long-term solvency ratio used to determine how a company's fixed assets are financed. It is calculated by dividing the value of net fixed assets (including trade investments) by the total long-term funds available to the business, which include share capital, reserves, and long-term loans.

Oct/Nov 2007

60. What does a Fixed Assets Ratio of more than 1 indicate?
(A) Short-term sources have been diverted for the creation of fixed assets.
(B) A part of the working capital has been successfully financed through long-term funds.
(C) The company has a very strong and stable long-term solvency position.
(D) The company's fixed assets are highly profitable and generating excellent returns.

Ans :

(A) Short-term sources have been diverted for the creation of fixed assets.
A Fixed Assets Ratio greater than 1 implies that fixed assets exceed the available long-term funds. This is an undesirable situation because it means that short-term sources of finance, such as current liabilities, have been used to acquire long-term assets. This creates a mismatch in maturity and can lead to liquidity problems.

May/June 2025

61. A Fixed Assets Ratio of less than 1 is considered desirable. What does it signify?
(A) The company has financed its fixed assets entirely with short-term debt and credit.
(B) The company is holding an excessive and inefficient amount of fixed assets.
(C) The company is facing imminent insolvency and potential bankruptcy proceedings.
(D) A portion of the working capital has been financed by long-term funds.

Ans :

(D) A portion of the working capital has been financed by long-term funds.
When the Fixed Assets Ratio is less than 1, it means that long-term funds are greater than the investment in fixed assets. The surplus of long-term funds is used to finance a part of the working capital. This is desirable as it supports the 'core working capital,' which is permanent in nature.

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Oct/Nov 2019

62. What is considered a satisfactory level for the Fixed Assets Ratio?
(A) Exactly 1
(B) 0.67 and below
(C) More than 1
(D) Between 1.2 and 2

Ans :

(B) 0.67 and below
While a ratio below 1 is generally desirable, the text specifies that a ratio of 0.67 and below is considered to be satisfactory. This indicates a healthy margin where a significant portion of long-term funds is available to finance the permanent or core component of the company's working capital, enhancing financial stability.

May/June 2009

63. For calculating the Fixed Assets Ratio, what do 'Long-term funds' include?
(A) The sum of current assets and current liabilities only.
(B) Share capital, reserves, and long-term loans.
(C) Only shareholders' equity and retained earnings.
(D) Total assets minus all current and long-term liabilities.

Ans :

(B) Share capital, reserves, and long-term loans.
The denominator of the Fixed Assets Ratio, 'Long-term funds', represents the pool of capital available for long-term purposes. As defined in the text, this includes the sum of share capital (both equity and preference), all reserves and surplus, and long-term loans or borrowings. It represents the total permanent capital of the firm.

Oct/Nov 2011

64. What is another name for the Debt-equity Ratio?
(A) Current Ratio
(B) Acid-Test Ratio
(C) External-Internal equity ratio
(D) Return on Investment

Ans :

(C) External-Internal equity ratio
The Debt-equity ratio is also known as the 'External-Internal' equity ratio. This name reflects its core function: comparing the funds provided by external parties (creditors or lenders, i.e., 'debt' or 'external equities') with the funds provided by the owners of the company (shareholders, i.e., 'equity' or 'internal equities').

May/June 2010

65. In the general calculation of the Debt-equity ratio, what does the term 'external equities' refer to?
(A) Total outside liabilities
(B) Shareholders' funds
(C) Long-term borrowings only
(D) Total assets

Ans :

(A) Total outside liabilities
When using the general formula for the Debt-equity ratio, the numerator is 'external equities'. This term is defined as the total liabilities owed to outsiders, which includes both long-term and short-term debt. It represents all claims on the company's assets by non-owners, contrasting with 'internal equities' or shareholders' funds.

Oct/Nov 2024

66. Which method of calculating the long-term financial Debt-equity ratio is stated to be the most popular?
(A) $\frac{\text{Total long} - \text{term debt}}{\text{Total long} - \text{term funds}}$
(B) $\frac{\text{External equities}}{\text{Internal equities}}$
(C) $\frac{\text{Total long} - \text{term debt}}{\text{Share holder's funds}}$
(D) $\frac{\text{Total debt}}{\text{Total assets}}$

Ans :

(C) $\frac{\text{Total long} - \text{term debt}}{\text{Share holder's funds}}$

The text presents two methods for calculating the debt-equity ratio as a long-term financial ratio. It explicitly states that Method (ii), which calculates the ratio as Total long-term debt divided by Shareholders' funds (tangible net worth), is the most popular method used in financial analysis.

May/June 2017

67. What is considered an ideal Debt-equity ratio when calculated as Total long-term debt to Shareholders' funds?
(A) 0.5
(B) 1
(C) 2
(D) 1.5

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Ans :

(B) 1

When using the popular method of dividing total long-term debt by shareholders' funds, an ideal ratio is considered to be 1. This signifies that the long-term borrowed funds are equal to the shareholders' funds (owned funds). This represents a balanced capital structure between debt and equity financing for long-term needs.

Oct/Nov 2005

68. In which type of business might a higher Debt-equity ratio be considered not unsatisfactory?

(A) A public utility concern.
(B) A software development startup.
(C) A retail clothing store.
(D) A professional consulting firm.

Ans :

(A) A public utility concern.

The text notes that while a 1:1 ratio is often ideal, a higher ratio (e.g., two-thirds borrowed funds to one-third owned funds) might be acceptable in certain cases. This is particularly true for businesses like public utility concerns, which typically have heavy investments in fixed assets and an assured, stable return on their investments.

May/June 2020

69. For the purpose of calculating the Debt-equity ratio, how should preference shares redeemable within twelve years from their issue date be treated?

(A) As a part of the shareholders' equity.
(B) As a fictitious asset to be written off.
(C) As a part of debt.
(D) They should be completely ignored in the calculation.

Ans :

(C) As a part of debt.

The text provides a specific rule for classifying certain preference shares. It states that preference shares that are redeemable within a period of twelve years from their date of issue should be considered as part of debt, not equity. This is because their fixed redemption timeline makes them more akin to a liability than permanent capital.

Oct/Nov 2015

70. What is the primary significance of the Debt-equity ratio for creditors?

(A) It provides a margin of safety for their loans.
(B) It indicates the overall profitability of the company.
(C) It shows the speed at which inventory is sold to customers.
(D) It measures the direct return on shareholders' investment.

Ans :

(A) It provides a margin of safety for their loans.

The Debt-equity ratio is crucial for creditors as it indicates the proportion of owners' stake versus outsiders' stake. A lower ratio means a larger equity cushion, which provides a margin of safety for creditors. It shows the extent to which the business can withstand losses before the creditors' capital is at risk.

May/June 2013

71. What does the Current Ratio indicate?

(A) The firm's long-term solvency and ability to pay off all its debt.
(B) The overall profitability of the firm's assets in generating revenue.
(C) The efficiency of the firm's sales force in achieving sales targets.
(D) The firm's commitment to meet its short-term liabilities.

Ans :

(D) The firm's commitment to meet its short-term liabilities.

The Current Ratio is a primary short-term solvency or liquidity ratio. Its purpose is to measure a firm's ability to pay off its short-term liabilities (those due within a year) using its short-term assets (those expected to be converted to cash within a year). It is a key indicator of immediate financial health.

Oct/Nov 2021

72. How are Current Assets defined for the purpose of the Current Ratio?

(A) All assets that will not be sold or converted to cash within the next five years.
(B) Cash and other assets convertible into cash during the operating cycle (not more than a year).
(C) Only the cash held in hand and the balances maintained in bank accounts.

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been sold in a period.

Ans :

(B) Whether the investment in inventories is efficiently used.
The Stock (or Inventory) Turnover Ratio is an activity ratio that measures how many times a company's inventory is sold and replaced over a period. It indicates the efficiency of inventory management, explaining whether the level of investment in inventories is appropriate for the level of sales, or if it is excessive.

May/June 2022

83. What is the formula for the Stock Turnover Ratio?
(A) $\frac{\text{Average inventory}}{\text{Net sales}}$
(B) $\frac{\text{Net sales}}{\text{Average inventory}}$
(C) $\frac{\text{Cost of goods sold during the year}}{\text{Average inventory}}$
(D) $\frac{\text{Average inventory}}{\text{Cost of goods sold during the year}}$

Ans :

(C) $\frac{\text{Cost of goods sold during the year}}{\text{Average inventory}}$

The Stock Turnover Ratio is calculated by dividing the cost of goods sold (COGS) during a specific period by the average inventory for that same period. Using COGS in the numerator is preferred over sales because COGS is valued at cost, just as inventory is, making the comparison more consistent.

Oct/Nov 2023

84. How can average inventory be computed if monthly stock levels are not available?
(A) By taking the inventory value at the end of the accounting period only.
(B) By taking the inventory value at the beginning of the accounting period only.
(C) By estimating the average based on the total sales figures for the period.
(D) On the basis of the average of inventory at the beginning and at the end of the accounting period.

Ans :

(D) On the basis of the average of inventory at the beginning and at the end of the accounting period.
The most accurate way to calculate average inventory is to average the monthly closing balances. However, if that data is unavailable, a common and acceptable alternative is to compute the average by taking the sum of the inventory at the beginning and the end of the accounting period and dividing it by two.

May/June 2016

85. What does a high inventory turnover ratio generally signify?
(A) Brisk sales and good inventory management.
(B) Significant blocking of funds in unsold inventory.
(C) A high risk of inventory becoming obsolete or outdated.
(D) Overvaluation of closing inventory on the balance sheet.

Ans :

(A) Brisk sales and good inventory management.
A high inventory turnover ratio signifies good liquidity of the inventory. It indicates that the company is selling its goods quickly, which minimizes the amount of capital tied up in stock. This generally points to brisk sales and efficient inventory management, reducing the risk of holding obsolete or deteriorating goods.

Oct/Nov 2009

86. What is the potential negative consequence of a low inventory turnover ratio?
(A) Frequent stock-outs and loss of potential sales.
(B) Blocking of funds and risk of inventory obsolescence.
(C) Excessively high storage and insurance costs.
(D) Artificially inflated company profits due to holding gains.

Ans :

(B) Blocking of funds and risk of inventory obsolescence.
A low turnover ratio implies that inventory is sitting for a long period before being sold. This results in the blocking of funds that could be used elsewhere in the business. It also increases the risk of the inventory becoming obsolete, deteriorating in quality, or declining in value, potentially leading to heavy losses.

May/June 2023

87. Match List-I (Ratio Category) with List-II (Specific Ratio).
List-I

NODIA

May/June 2008

77. Which of the following is an alternative name for the Liquidity Ratio?
(A) Solvency Ratio
(B) Debt-equity Ratio
(C) Turnover Ratio
(D) Acid test ratio

Ans :

(D) Acid test ratio
The Liquidity Ratio is also commonly referred to as the 'acid test ratio' or 'quick ratio'. These names emphasize its more stringent test of a company's liquidity compared to the current ratio. It assesses the ability to meet current liabilities without relying on the sale of less liquid inventory.

Oct/Nov 2013

78. What is the formula for the Liquidity Ratio?
(A) $\frac{\text{Liquid assets}}{\text{Current liabilities}}$
(B) $\frac{\text{Current assets}}{\text{Current liabilities}}$
(C) $\frac{\text{Current assets}}{\text{Liquid assets}}$
(D) $\frac{\text{Liquid assets}}{\text{Total liabilities}}$

Ans :

(A) $\frac{\text{Liquid assets}}{\text{Current liabilities}}$
The Liquidity Ratio, also known as the quick or acid-test ratio, is calculated by dividing liquid assets by current liabilities. It provides a more conservative measure of liquidity than the current ratio by excluding assets that are not easily converted to cash.

May/June 2015

79. How are 'liquid assets' defined for the purpose of the quick ratio?
(A) All assets classified as current on the balance sheet.
(B) Only the cash held in hand and balances in bank accounts.
(C) Current assets other than inventory and prepaid expenses.
(D) The total of current assets minus the total of current liabilities.

Ans :

(C) Current assets other than inventory and prepaid expenses.
Liquid assets, also known as quick assets, are defined as those current assets that can be converted into cash almost immediately and without significant loss of value. For the purpose of this ratio, they are calculated by taking total current assets and subtracting inventory and prepaid expenses, which are considered the least liquid components.

Oct/Nov 2012

80. A quick ratio above what level may be considered satisfactory?
(A) 1
(B) 0.5
(C) 2
(D) 1.5

Ans :

(A) 1
A quick ratio of 1 indicates that the company has exactly one rupee of highly liquid assets for every one rupee of current liabilities. The text states that a quick ratio above 1 may be considered satisfactory, as it suggests the company can meet its current obligations without having to sell its inventory.

May/June 2011

81. If two firms have the same current ratio but different liquidity ratios, what does a lower liquidity ratio for one firm indicate?
(A) Better management of current liabilities.
(B) Significantly higher cash and bank balances.
(C) Faster collection of accounts receivable.
(D) Over-stocking or larger inventory hold-ups.

Ans :

(D) Over-stocking or larger inventory hold-ups.
The key difference between the current ratio and the liquidity ratio is the exclusion of inventory. If two firms have an identical current ratio, but one has a significantly lower liquidity ratio, it implies that a larger proportion of its current assets is tied up in inventory, suggesting potential over-stocking or inventory management issues.

Oct/Nov 2020

82. What does the Stock Turnover Ratio indicate?
(A) The overall profitability of the inventory held by the company.
(B) Whether the investment in inventories is efficiently used.
(C) The proportion of inventory that has been financed by debt.
(D) The total physical quantity of stock that has

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(D) The total assets of the company minus the value of its fixed assets and investments.

Ans :

(B) Cash and other assets convertible into cash during the operating cycle (not more than a year). Current assets are defined as cash and any other assets that are expected to be converted into cash, sold, or consumed during the business's normal operating cycle, which is typically not more than one year. This includes items like cash, marketable securities, accounts receivable, and inventory.

May/June 2024

73. Which of the following items should NOT be included in current assets when calculating the Current Ratio?

(A) Prepaid expenses for services to be received within the year.

(B) Cash held in hand and in current bank accounts.

(C) Book debts outstanding for more than six months.

(D) The inventory of finished goods ready for sale to customers.

Ans :

(C) Book debts outstanding for more than six months.

The text provides specific guidance on the composition of current assets for this ratio. It explicitly states that book debts (accounts receivable) that have been outstanding for more than six months, along with loose tools, should not be included. This is because their convertibility into cash within the short term is doubtful.

Oct/Nov 2008

74. What does a very high current ratio, such as 4:1, potentially indicate?

(A) Extremely efficient use of funds and exceptionally high profitability.

(B) A strong and clear signal to invest in the company's stock immediately.

(C) Less efficient or inadequate employment of funds.

(D) The company is facing a severe and immediate liquidity crisis.

Ans :

(C) Less efficient or inadequate employment of funds.

While a low current ratio is a danger signal, a very high one is also not desirable. It can indicate that funds are being used inefficiently. For example, it may suggest that too much cash is sitting idle or that there are excessive levels of inventory or debtors, representing underutilized assets that could be invested more productively.

May/June 2006

75. What is generally considered a satisfactory range for the Current Ratio?

(A) Between 1.2 and 2

(B) Less than 1

(C) Exactly 1

(D) More than 3

Ans :

(A) Between 1.2 and 2

While context matters, the text suggests a general benchmark for a satisfactory current ratio. A ratio falling between 1.2 and 2 is often considered acceptable. This range implies that the company has sufficient current assets to cover its current liabilities without having an excessive, unproductive amount of liquid assets on hand.

Oct/Nov 2017

76. What is the significance of the Current Ratio for a business?

(A) It is an index of the concern's financial stability.

(B) It is the primary measure of long-term profitability.

(C) It directly determines the credit rating of the company.

(D) It reflects the market's perception of growth prospects.

Ans :

(A) It is an index of the concern's financial stability.

The current ratio is considered an index of a company's financial stability because it measures the extent to which current assets cover current liabilities. This difference, known as working capital, provides a buffer for meeting day-to-day obligations. A healthy ratio suggests the firm is stable enough to manage its short-term financial commitments.

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P. Profitability Ratio
Q. Long-term Solvency Ratio
R. Short-term Solvency Ratio
S. Turnover Ratio

List-II
1. Current Ratio
2. Stock Turnover Ratio
3. Gross Profit Ratio
4. Debt-Equity Ratio

(A) P-3, Q-4, R-1, S-2
(B) P-1, Q-2, R-3, S-4
(C) P-3, Q-1, R-4, S-2
(D) P-2, Q-4, R-1, S-3

Ans :

(A) P-3, Q-4, R-1, S-2
The Gross Profit Ratio is a Profitability Ratio (P-3). The Debt-Equity Ratio measures Long-term Solvency (Q-4). The Current Ratio measures Short-term Solvency (R-1). The Stock Turnover Ratio is a Turnover or activity ratio (S-2). This matching correctly aligns each specific ratio with its functional classification as described in the chapter.

Oct/Nov 2018

88. What two ratios are used by financial analysts to judge the quality of a firm's debtors?
(A) Debtors' turnover ratio and Debt collection period ratio
(B) Current ratio and Quick ratio
(C) Gross profit ratio and Net profit ratio
(D) Debt-equity ratio and Fixed assets ratio

Ans :

(A) Debtors' turnover ratio and Debt collection period ratio
The quality of debtors is crucial for a firm's liquidity. To assess this, analysts use two primary ratios: the Debtors' Turnover Ratio (also known as Debtors' Velocity), which measures how quickly credit sales are converted into cash, and the Debt Collection Period Ratio, which calculates the average time it takes to collect payments.

May/June 2007

89. What is the standard formula for the Debtors' Turnover Ratio?
(A) $\frac{\text{Total sales}}{\text{Average accounts receivable}}$
(B) $\frac{\text{Average accounts receivable}}{\text{Credit sales}}$
(C) $\frac{\text{Credit sales}}{\text{Average accounts receivable}}$
(D) $\frac{\text{Cash sales}}{\text{Average accounts receivable}}$

Ans :

(C) $\frac{\text{Credit sales}}{\text{Average accounts receivable}}$
The Debtors' Turnover Ratio is designed to measure the efficiency of collecting credit sales. Therefore, the most accurate formula uses Credit Sales in the numerator and compares it to the Average Accounts Receivable for the period. Using total sales can distort the ratio if cash sales are significant.

Oct/Nov 2025

90. What is included in the term 'Accounts Receivable' for calculating the debtors' turnover ratio?
(A) Trade Debtors and Bills Receivable
(B) Only Trade Debtors
(C) Only Bills Receivable
(D) All current assets

Ans :

(A) Trade Debtors and Bills Receivable
The term 'Accounts Receivable' is a comprehensive term that represents the total amount owed to a company by its customers from credit sales. For the purpose of ratio calculation, it includes both 'Trade Debtors' (amounts owed on open accounts) and 'Bills Receivable' (amounts formalized through promissory notes or bills of exchange).

May/June 2012

91. A higher Debtors' Turnover Ratio is generally better. What does it indicate?
(A) The company is following a very liberal and lenient credit policy.
(B) The company's total sales are likely declining year over year.
(C) The company is experiencing a high and rising level of bad debts.
(D) The staff entrusted with collection of book debts is efficient.

Ans :

(D) The staff entrusted with collection of book debts is efficient.
A higher Debtors' Turnover Ratio indicates that debts are being collected more promptly. This efficiency is often attributed to the effectiveness of the staff or department responsible for managing

NODIA

The Gross Profit Ratio is calculated to show the percentage of sales revenue that is left after subtracting the cost of goods sold. The formula is Gross Profit divided by Net Sales, with the result multiplied by 100. This ratio is a key indicator of a company's production and pricing efficiency.

May/June 2021

53. What does the Gross Profit Ratio primarily indicate?

(A) The overall profitability of the business after all expenses and taxes have been paid.
(B) The company's ability to meet its short-term obligations as they become due.
(C) The degree to which the selling price of goods can decline without causing an operating loss.
(D) The efficiency of asset utilization in generating sales revenue for the company.

Ans :

(C) The degree to which the selling price of goods can decline without causing an operating loss.
The significance of the Gross Profit Ratio lies in its ability to show the margin available to cover other expenses. It indicates the cushion or degree to which the selling price per unit can fall before the company starts incurring losses from its core operations. It also helps in monitoring the average markup on goods.

Oct/Nov 2010

54. According to the text, what should the gross profit be adequate to cover?

(A) Only the cost of goods sold and direct production expenses.
(B) Only the interest payments on long-term debt and debentures.
(C) Only the capital expenditure for purchasing new fixed assets.
(D) Operating expenses, fixed charges, dividends, and building up of reserves.

Ans :

(D) Operating expenses, fixed charges, dividends, and building up of reserves.
While there is no fixed norm for the Gross Profit Ratio, it is a matter of judgment. However, the gross profit generated must be sufficient to cover all other business costs, including operating expenses, fixed charges like interest, payments to shareholders (dividends), and the retention of earnings for future growth (building up of reserves).

May/June 2005

55. What does the Net Profit Ratio indicate?

(A) The net margin earned on a sale of ₹100.
(B) The gross margin earned on a sale of ₹100.
(C) The asset turnover rate of the company for a given period.
(D) The specific return on equity for the common shareholders.

Ans :

(A) The net margin earned on a sale of ₹100.
The Net Profit Ratio is calculated as

$$\frac{\text{Net operating profit}}{\text{Net sales}} \times 100$$

It indicates the net margin or the final profit earned for every ₹100 of sales after all operating costs have been accounted for. It is a measure of the overall profitability and efficiency of the business management.

Oct/Nov 2022

56. An increase in the Net Profit Ratio over the previous period, provided the Gross Profit Ratio is constant, indicates what?

(A) A significant decline in the operational efficiency of the business.
(B) An improvement in the operational efficiency of the business.
(C) A decision by the company to take on substantially more debt.
(D) A large and unexpected decrease in the company's sales volume.

Ans :

(B) An improvement in the operational efficiency of the business.
If the Gross Profit Ratio remains constant, it means the margin on sales before operating expenses is unchanged. Therefore, an increase in the Net Profit Ratio must be due to better management of operating expenses (like administrative and selling costs). This points to an improvement in the overall operational efficiency of the business.

May/June 2018

57. Which of the following is NOT a factor an investor should consider when judging the adequacy of the Net Profit Ratio?

(A) The cost of capital.
(B) The return in the industry as a whole.

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(B) Three to four months

While it is difficult to set a universal standard, the text provides a general guideline for managing receivables. It suggests that, in general, the total amount of accounts receivable outstanding at any time should not be more than the value of three to four months' worth of credit sales for the firm.

May/June 2005

97. Which ratio would a long-term creditor be most interested in to assess a company's ability to pay interest charges?

(A) Quick ratio
(B) Fixed charges cover ratio
(C) Earnings per share
(D) Dividend yield ratio

Ans :

(B) Fixed charges cover ratio

A long-term creditor is primarily concerned with the company's ability to meet its long-term obligations, especially fixed interest payments.

The Fixed Charges Cover Ratio, calculated as

$$\frac{\text{Income before interest and tax}}{\text{Interest charges}}$$

Directly measures how many times the company's earnings can cover its interest expenses, indicating the safety margin for the creditor.

Oct/Nov 2022

98. What is the formula for the Debt Service Coverage Ratio (DSCR)?

(A) $\frac{\text{Cash profit available for debt service}}{\text{Interest + Principal payments instalment}}$

(B) $\frac{\text{Interest + Principal payments instalment}}{\text{Cash profit available for debt service}}$

(C) $\frac{\text{Net Profit}}{\text{Total Debt}}$

(D) $\frac{\text{Operating Profit}}{\text{Interest Charges}}$

Ans :

(A) $\frac{\text{Cash profit available for debt service}}{\text{Interest + Principal payments instalment}}$

The Debt Service Coverage Ratio (DSCR) is a comprehensive measure used by lenders to assess a company's ability to service its debt. It compares the cash profit available for debt servicing to the total debt obligation for the period, which includes both interest charges and the principal repayment instalment.

May/June 2018

99. Which two ratios are of primary importance to a bank when considering granting a short-term loan?

(A) Debt-equity ratio and Fixed assets ratio
(B) Earnings per share and P/E ratio
(C) Quick ratio and Current ratio
(D) Gross profit ratio and Net profit ratio

Ans :

(C) Quick ratio and Current ratio

A bank granting a short-term loan is most concerned with the borrower's ability to repay the loan in the near future. The Current Ratio and the Quick (or Acid-Test) Ratio are the key indicators of short-term liquidity. They measure the company's capacity to meet its immediate obligations using its liquid assets.

Oct/Nov 2016

100. Which ratio would a shareholder use to assess the return on their investment based on the current share price?

(A) Dividend yield ratio
(B) Earnings per share
(C) Debt service coverage ratio
(D) Fixed charges cover ratio

Ans :

(A) Dividend yield ratio

The Dividend Yield Ratio, calculated as

$$\frac{\text{Dividend per share}}{\text{Market price per share}}$$

Shows the return a shareholder receives in the form of dividends as a percentage of the current market price of the share. It is a key metric for investors focused on income generation from their stock holdings.

May/June 2014

101. Based on the source, "Ratios are only indicators; they cannot be taken as final regarding good or bad financial position of the business. Other things have also to be seen. For example, a high current ratio does not necessarily mean that the concern has a good liquid position, in case the current assets mostly comprise of outdated stocks," which conclusion is most appropriate?

(A) A high current ratio is always a definitive and conclusive indicator of a strong liquid position.
(B) The entire practice of ratio analysis becomes invalid if a company holds any outdated

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(D) To adjust financial accounts to accurately reflect the impact of price-level changes.

Ans :

(A) To create a deceptively favorable impression of the company's financial health.
The source defines window dressing as manipulating accounts to hide crucial facts and present a position that appears "better than what actually is." This clearly indicates that the objective is not accuracy or simplicity, but deception. The goal is to mislead users of financial statements into believing the company is in a stronger position than reality.

May/June 2017

109. What is the main criticism of the traditional classification of ratios according to the source: "Traditional basis of classification... has been found to be too crude and unsuitable because, analysis of balance sheet and income statement cannot be done in isolation. They have to be studied together in order to determine the profitability and solvency of the business."?
(A) It generates far too many individual ratios to be of any practical use to an analyst.
(B) It relies on outdated accounting principles that are no longer in common use.
(C) It separates the analysis of statements that should be analyzed jointly.
(D) It is a system that is only applicable to non-profit and governmental organizations.

Ans :

(C) It separates the analysis of statements that should be analyzed jointly.
The source explicitly states that the traditional classification is unsuitable because the balance sheet and income statement "cannot be done in isolation." It emphasizes that they "have to be studied together" to assess profitability and solvency. This directly points to the flaw of separating the analysis of interconnected financial statements, which the functional classification seeks to rectify.

Oct/Nov 2005

110. According to the source, "In order to measure a firm's credit and collection efficiency, its average collection period should be compared with the average of the industry. It should be neither too liberal nor too restrictive," what is the best way to evaluate a firm's average collection period?
(A) By benchmarking it against the industry average and seeking a balanced approach.
(B) By ensuring it is as short as possible, ideally aiming for zero days in all cases.
(C) By comparing it only against the firm's own historical performance over several years.
(D) By ensuring it does not exceed the credit period granted by the firm's own suppliers.

Ans :

(A) By benchmarking it against the industry average and seeking a balanced approach.
The source provides two key evaluation criteria. First, it recommends comparing the firm's collection period with the industry average to gauge relative performance. Second, it advises against extremes, stating the policy should be "neither too liberal nor too restrictive." This supports the idea of using an industry benchmark and aiming for a balanced, moderate policy.

May/June 2020

111. A company has current assets of ₹20,000 and current liabilities of ₹10,000. It makes a payment of ₹5,000 to a current creditor from its cash balance. What is the effect on the current ratio?
(A) The ratio will improve from 2:1 to 3:1.
(B) The ratio will decline from 2:1 to 1.5:1.
(C) The ratio will remain unchanged at 2:1.
(D) The ratio will decline from 2:1 to 1:1.

Ans :

(A) The ratio will improve from 2:1 to 3:1.
The initial current ratio is

$$\frac{20,000}{10,000} = 2$$

After paying the creditor, current assets decrease to ₹15,000 (20,000 - 5,000) and current liabilities decrease to ₹5,000 (10,000 - 5,000).
The new current ratio is

$$\frac{15,000}{5,000} = 3$$

Thus, the ratio improves from 2:1 to 3:1.

Oct/Nov 2015

112. A firm with a current ratio of 2:1 purchases fixed assets for cash. What will be the immediate impact on its current ratio?
(A) It will improve.
(B) It will decline.
(C) It will remain unchanged.
(D) It will become zero.

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Total long-term debt to Shareholders' funds. This directly answers the question based on the information given in the source text.

May/June 2009

105. In the context of the source, "A low inventory turnover ratio results in the blocking of funds in inventory, which may ultimately result in heavy losses due to inventory becoming obsolete or deteriorating in quality. The stock position is known as the graveyard of the balance sheet," what does the phrase "graveyard of the balance sheet" refer to?

(A) The potential for inventory to become a source of major financial loss and write-offs.
(B) The specific section of the balance sheet where fixed assets are listed and depreciated.
(C) A company that has already gone bankrupt primarily due to poor sales performance.
(D) The formal accounting entry required for writing off obsolete or damaged stock.

Ans :

(A) The potential for inventory to become a source of major financial loss and write-offs.
The source uses the dramatic phrase "graveyard of the balance sheet" to describe the stock position. This is used in the context of a low turnover ratio, where inventory can become obsolete or deteriorate, leading to heavy losses. The phrase metaphorically represents where asset value (from inventory) goes to "die" or be written off.

Oct/Nov 2011

106. According to the source, "The ratio [Debt Collection Period] is very helpful to the lenders because it explains to them whether their borrowers are collecting money within a reasonable time. An increase in the period will result in greater blockage of funds in debtors," why is the Debt Collection Period particularly useful for lenders?

(A) It helps them set the final interest rate and terms for the loan agreement.
(B) It shows if the borrower is efficiently managing a key component of its working capital.
(C) It provides a direct indication of the borrower's overall profitability and net income.
(D) It guarantees that the borrower will be able to repay the loan principal on time.

Ans :

(B) It shows if the borrower is efficiently managing a key component of its working capital.
The source states the ratio is helpful to lenders because it shows if the borrower is collecting its own debts in a reasonable time. This is a direct measure of working capital management. A failure to collect receivables efficiently (a longer period) means funds are blocked, which could impair the borrower's ability to service its own debt to the lender.

May/June 2010

107. What fundamental condition for business survival is stated in this source: "The business can survive only when the return on capital employed is more than the cost of capital employed in the business."?

(A) A company must generate more total revenue than its total expenses.
(B) The company's total assets must be greater than its total liabilities.
(C) The company must achieve a positive cash flow from operations each year.
(D) The rate of profit from investments must exceed the rate paid for the funds used.

Ans :

(D) The rate of profit from investments must exceed the rate paid for the funds used.
The source establishes a clear benchmark for survival. "Return on capital employed" is the profit rate from investments, and "cost of capital employed" is the rate paid for those funds (e.g., interest on debt). The statement mandates that the former must be greater than the latter, meaning the business must earn more on its capital than it costs.

Oct/Nov 2024

108. Based on this definition, "The term window dressing means manipulation of accounts in such a way, as to conceal vital facts and, present the financial statements in such a way, as to show a better position than what actually is," what is the ultimate goal of window dressing?

(A) To create a deceptively favorable impression of the company's financial health.
(B) To ensure full and transparent compliance with all relevant accounting standards.
(C) To translate complex financial data into a simplified format for average investors.

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stock.
(C) According to accounting rules, outdated stocks must always be formally excluded from the current ratio calculation.
(D) Ratios must be interpreted in conjunction with an analysis of the quality of the underlying assets.

Ans :

(D) Ratios must be interpreted in conjunction with an analysis of the quality of the underlying assets.
The source text explicitly warns that a high current ratio is not conclusive proof of good liquidity. The reason given is that the composition and quality of the assets matter, citing outdated stocks as an example. This directly supports the conclusion that ratios require qualitative interpretation of the underlying assets, not just mechanical calculation.

Oct/Nov 2007

102. According to the source, "The term 'Operating Profit' means profit before 'Interest and Tax'. The term 'Interest' means 'Interest on long-term borrowings'. Interest on short-term borrowings will be deducted for computing operating profit. Non-trading incomes such as interest on Government securities or non-trading losses or expenses such as loss on account of fire, etc. will also be excluded...," which item is deducted when calculating Operating Profit for ROI?
(A) Interest on long-term borrowings
(B) Interest on short-term borrowings
(C) Income tax
(D) Loss on account of fire

Ans :

(B) Interest on short-term borrowings
The source clearly defines Operating Profit as profit before interest on long-term borrowings and tax. However, it makes a specific distinction, stating that interest on short-term borrowings will be deducted. It also states non-trading items like loss on fire are excluded, not deducted from an operating base. Thus, short-term interest is treated as an operating expense.

May/June 2025

103. What is the justification provided in the source, "A ratio of less than 1 [for the Fixed Assets Ratio] shows that a part of the working capital has been financed through long-term funds. This is desirable because a part of working capital, termed as 'core working capital', is more or less of a fixed nature," for desiring a Fixed Assets Ratio of less than 1?
(A) It indicates that all of the company's fixed assets have been financed by equity.
(B) It proves conclusively that the company has no outstanding short-term debt.
(C) It shows that long-term funds are being used to support the permanent portion of working capital.
(D) It ensures that the company's fixed assets are generating a high return on investment.

Ans :

(C) It shows that long-term funds are being used to support the permanent portion of working capital.
The source directly links a Fixed Assets Ratio below 1 to the financing of working capital. It states this is desirable because the excess long-term funds are used to finance 'core working capital,' which is the permanent, fixed-nature component of working capital. This aligns the maturity of funds with the nature of the assets being financed.

Oct/Nov 2019

104. "In case debt-equity ratio is to be calculated as a long-term financial ratio, it may be calculated as follows:
(i) Total long-term debt / Total long-term funds.
(ii) Total long-term debt / Shareholders' funds.
Method (ii) is most popular," what is the most popular way to compute the long-term debt-equity ratio?
(A) By dividing total long-term debt by shareholders' funds.
(B) By dividing total long-term debt by the company's total assets.
(C) By dividing total debt, including current liabilities, by total equity.
(D) By dividing total long-term debt by the sum of long-term debt and shareholders' funds.

Ans :

(A) By dividing total long-term debt by shareholders' funds.
The source presents two specific methods for calculating the long-term debt-equity ratio. It then explicitly states that "Method (ii) is most popular." Method (ii) is defined as the ratio of

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Ans :

(B) It will decline.
Let's assume initial current assets are ₹20,000 and current liabilities are ₹10,000 (Ratio = 2). Purchasing fixed assets for cash reduces current assets (cash decreases) but has no effect on current liabilities. For example, a ₹5,000 purchase would make current assets ₹15,000.
The new ratio would be

$$\frac{15,000}{10,000} = 1.5$$

Which is a decline.

May/June 2013

113. A company has a current ratio of 2:1. It collects cash from its debtors. What is the effect on the current ratio?
(A) The ratio will improve.
(B) The ratio will decline.
(C) The ratio will remain unchanged.
(D) The effect cannot be determined.

Ans :

(C) The ratio will remain unchanged.
Collecting cash from debtors involves the conversion of one current asset (debtors) into another current asset (cash). This transaction changes the composition of current assets but does not change the total amount of current assets. Since current liabilities are also unaffected, the current ratio will remain unchanged.

Oct/Nov 2021

114. A firm has a current ratio of 2:1. A bill receivable is dishonoured, and it is assumed the customer is solvent. What is the impact on the current ratio?
(A) It will decline because bad debts increase.
(B) It will improve because debtors increase.
(C) It will decline because current liabilities increase.
(D) It will remain unchanged because one current asset is replaced by another.

Ans :

(D) It will remain unchanged because one current asset is replaced by another.
When a bill receivable is dishonoured and the customer is solvent, the amount is transferred from 'Bills Receivable' to 'Sundry Debtors'. Both are current assets. This transaction merely changes the form of the current asset without altering the total value of current assets or current liabilities. Therefore, the current ratio remains unchanged.

May/June 2024

115. A company with a current ratio of 2:1 issues new shares for cash. What is the consequential effect on the current ratio?
(A) It will improve.
(B) It will decline.
(C) It will remain unchanged.
(D) It will become negative.

Ans :

(A) It will improve.
Issuing new shares for cash increases the company's cash balance, which is a current asset. This transaction does not affect current liabilities. An increase in the numerator (current assets) with the denominator (current liabilities) remaining constant will lead to a consequential improvement or increase in the current ratio.

Oct/Nov 2008

116. A firm has a current ratio of 2:1. If it issues new shares in consideration for the purchase of fixed assets, what is the impact on the current ratio?
(A) It will improve.
(B) There will be no change.
(C) It will decline.
(D) It will double.

Ans :

(B) There will be no change.
This transaction involves an increase in fixed assets (a non-current asset) and an increase in share capital (equity). It has no impact on either current assets or current liabilities. Since both the numerator and the denominator of the current ratio formula remain unaffected, the ratio itself will have no change.

May/June 2006

117. A company's current assets are ₹40,000 and its current liabilities are ₹20,000. It then purchases goods worth ₹10,000 on credit. What is the new current ratio?
(A) 2:1
(B) 1.67:1
(C) 3:1
(D) 1.5:1

Ans :

(B) 1.67:1

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CHAPTER 21

Financial Mathematics – Calculation of Interest & Annuities

May/June 2019

1. According to the objectives of the unit, which of the following is a key area of understanding in financial mathematics for bankers?

(A) The qualitative theories behind stock market fluctuations and complex methods for equity valuation.

(B) The fundamental mathematical calculations for simple interest, compound interest, annuities, and sinking funds.

(C) The detailed regulatory framework governing international trade finance and foreign exchange risk management.

(D) The advanced statistical models and machine learning techniques used for credit risk assessment in corporate lending.

Ans :

(B) The fundamental mathematical calculations for simple interest, compound interest, annuities, and sinking funds.

The unit's objectives explicitly state the aim is to understand the mathematical calculations for simple and compound interest, annuities, and sinking funds. It also covers the application of these mathematical concepts within the banking industry, which forms the core focus of the chapter, distinct from equity valuation or regulatory frameworks.

Oct/Nov 2023

2. What is the primary reason for a bank to perform a cost-benefit analysis of a series of annuities?

(A) To determine the present value of future annuity payments and compare it with the initial cash outflow for decision-making.

(B) To establish the new prime lending rate for the upcoming financial quarter based on forecasted market conditions.

(C) To ensure full compliance with the international Basel III norms for maintaining minimum capital adequacy ratios.

(D) To decide upon the optimal dividend payout ratio for its shareholders at the conclusion of the fiscal year.

Ans :

(A) To determine the present value of future annuity payments and compare it with the initial cash outflow for decision-making.

Banks conduct cost-benefit analyses of annuities by calculating their present value. This involves discounting the future series of payments to their current worth. This present value is then compared against any immediate cash outflow or investment required, enabling the bank to make informed financial decisions regarding loans or investments structured as annuities.

May/June 2007

3. In the context of simple interest, what does the term 'Principal' refer to?

(A) The total cumulative amount of interest that is paid or received over the entire tenure of the loan.

(B) The final accumulated sum, including principal and all interest, at the end of the contracted period.

(C) The initial sum of money lent or borrowed which remains constant for interest calculation.

(D) The periodic service fee paid to the lender, which is separate from and excludes the original amount.

Ans :

(C) The initial sum of money lent or borrowed which remains constant for interest calculation.

The principal is the initial amount of money lent or borrowed. A key characteristic of simple interest calculation is that this principal amount remains constant throughout the entire loan period. Interest is calculated exclusively on this

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(A) The Debt-equity ratio is also known as the 'External-Internal' equity ratio.
(B) The Liquidity Ratio is also termed as the 'current ratio'.
(C) A Fixed Assets Ratio of more than 1 indicates diversion of short-term funds for long-term assets.
(D) A high stock turnover ratio is generally an indicator of operational efficiency.

Ans :

(B) The Liquidity Ratio is also termed as the 'current ratio'.
This statement is incorrect. The Liquidity Ratio is also termed the 'acid test ratio' or 'quick ratio'. The 'current ratio' is a separate, less stringent measure of liquidity. While both are short-term solvency ratios, they are distinct measures and not alternative names for each other, as they use different components for calculation.

May/June 2011

123. **Assertion (A) :** A very high current ratio is not always a good sign for a business.
Reason (R) : It may indicate that funds are inadequately employed, for instance, through idle cash or outdated stocks.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is true; a very high current ratio can be undesirable. Reason (R) correctly explains why: it can signify inefficient use of assets. For example, excessive cash is not earning a return, and high levels of outdated stock represent tied-up capital with a risk of loss, indicating inadequate employment of funds.

Oct/Nov 2020

124. **Assertion (A) :** Comparison of ratios between two companies can be misleading.
Reason (R) : Different companies may adopt different accounting policies for items like depreciation and inventory valuation.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is a stated limitation of ratio analysis. Reason (R) provides the primary justification for this limitation. Because companies can choose different accounting policies, the resulting profit and asset figures are not directly comparable. This lack of a like-for-like basis makes a simple comparison of their ratios potentially meaningless or misleading.

May/June 2022

125. Identify the correct statement regarding the limitations of ratio analysis.
(A) Ratios can give misleading results if the effects of price level changes are not considered.
(B) Ratios are self-sufficient and do not require comparison with past results or industry benchmarks.
(C) Ratios are unaffected by "window dressing" or manipulation of accounts.
(D) Ratios incorporate all non-financial factors, such as the quality of management.

Ans :

(A) Ratios can give misleading results if the effects of price level changes are not considered.
The text clearly lists the problems of price level changes as a significant limitation. Comparing firms from different eras without adjusting for inflation can distract figures for assets and depreciation, leading to misleading conclusions. The other options describe situations that are the opposite of the limitations discussed; ratios do require comparison, are affected by window dressing, and exclude non-financial factors.

Oct/Nov 2023

126. Match List-I (Ratio) with List-II (Formula).
List-I
P. EPS
Q. P/E Ratio
R. Net Profit Ratio
S. Fixed Assets Ratio
List-II
1. $\frac{\text{Market price per equity share}}{\text{Earning per share}}$

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Initially, the ratio is

$$\frac{40,000}{20,000} = 2$$

The credit purchase increases inventory (a current asset) by ₹10,000 and creditors (a current liability) by ₹10,000. New current assets are ₹50,000 and new current liabilities are ₹30,000.
The new ratio is

$$\frac{50,000}{30,000} = 1.67.$$

Oct/Nov 2017

118. A company has a quick ratio of 1.5:1, with current liabilities of ₹50,000. Its inventory is valued at ₹25,000. What is the company's current ratio?
(A) 2:1
(B) 2.5:1
(C) 1.5:1
(D) 1:1

Ans :

(A) 2:1

$$\text{Quick Ratio} = \frac{\text{Quick Assets}}{\text{Current Liabilities}}.$$

So,
Quick Assets = 1.5 × ₹ 50,000 = ₹ 75,000.
Current Assets = Quick Assets + Inventory.
So,
Current Assets = ₹ 75,000 + ₹ 25,000 = ₹ 100,000.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$= \frac{100,000}{50,000} = 2.$$

The current ratio is 2:1.

May/June 2008

119. A firm's net profit after tax and preference dividend is ₹5,00,000. It has 1,00,000 outstanding equity shares, and the current market price per share is ₹60. What is the firm's P/E ratio?
(A) 10
(B) 8
(C) 12
(D) 15

Ans :

(C) 12
First, calculate the Earnings Per Share (EPS).

$$\text{EPS} = \frac{\text{Net Profit available to equity share holders}}{\text{Number of equity shares}}$$

$$= \frac{5,00,000}{1,00,000} = 5$$

The P/E Ratio = Market Price per Share / EPS.

$$= \frac{60}{5} = 12.$$

The Price-Earnings ratio of the firm is 12.

Oct/Nov 2013

120. A bill receivable of ₹10,000 held by a company with a 2:1 current ratio is dishonoured. The company anticipates the debt will become bad and records it as such. What is the impact on the current ratio?
(A) The ratio will fall.
(B) The ratio will remain unchanged.
(C) The ratio will improve.
(D) The ratio will become 1:1.

Ans :

(A) The ratio will fall.
Initially, the bill receivable is a current asset. When it is dishonoured and recorded as a bad debt, the value of current assets is reduced by ₹10,000 (as the receivable is written off). Current liabilities remain unchanged. A reduction in the numerator (current assets) while the denominator stays the same will cause the ratio to fall.

May/June 2015

121. Consider the following statements about accounting ratios:
1. Ratios can be classified on a traditional basis or a functional basis.
2. Under functional classification, ratios are grouped as Profitability, Turnover, and Solvency.
3. Traditional classification is considered more suitable for modern analysis.

Which of the above statements is/are correct?
(A) 1 only
(B) 1 and 2 only
(C) 2 and 3 only
(D) 1, 2 and 3

Ans :

(B) 1 and 2 only
The text confirms that ratios can be classified traditionally (by statement) or functionally (by purpose). It also lists Profitability, Turnover, and Solvency as the main functional categories. However, it explicitly states that the traditional classification is "too crude and unsuitable" for modern analysis, making statement 3 incorrect. Therefore, only statements 1 and 2 are correct.

Oct/Nov 2012

122. Which of the following statements is incorrect?

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Liquidity Ratio $= \frac{1,50,000}{1,00,000} = 1.5$.

The ratio is therefore 1.5:1.

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2. $\frac{\text{Net operating profit}}{\text{Net sales}} \times 100$
3. $\frac{\text{Fixed assets}}{\text{Long} - \text{term funds}}$
4. $\frac{\text{Net profit after tax and pref. dividend}}{\text{Number of equity shares}}$

(A) P-1, Q-4, R-2, S-3
(B) P-4, Q-1, R-3, S-2
(C) P-4, Q-1, R-2, S-3
(D) P-2, Q-3, R-1, S-4

Ans :

(C) P-4, Q-1, R-2, S-3
The correct formula for Earnings Per Share (EPS) is given in 4. The Price Earning (P/E) Ratio is correctly defined in 1. The Net Profit Ratio formula is correctly stated in 2. The Fixed Assets Ratio formula is correctly shown in 3. Therefore, the combination P-4, Q-1, R-2, S-3 correctly matches each ratio with its corresponding formula.

May/June 2016

127. Consider the following statements:
1. A poor current ratio is a danger signal to management.
2. A high current ratio always indicates efficient use of funds.
3. A current ratio of between 1.2 and 2 may be considered satisfactory.

Which of the above statements is/are correct?
(A) 1 only
(B) 1 and 3 only
(C) 2 and 3 only
(D) 1, 2 and 3

Ans :

(B) 1 and 3 only
The text states that a poor current ratio is a danger signal. It also suggests a range of 1.2 to 2 may be satisfactory. However, it explicitly warns that a very high current ratio is not desirable as it can mean less efficient use of funds. Therefore, statement 2 is incorrect.

Oct/Nov 2009

128. Which of the following pairs is incorrectly matched?
(A) ROI : Overall Profitability Ratio
(B) Liquidity Ratio : Acid Test Ratio
(C) Stock Turnover Ratio : Solvency Ratio
(D) Debt-Equity Ratio : External-Internal equity ratio

Ans :

(C) Stock Turnover Ratio : Solvency Ratio
The Stock Turnover Ratio is a measure of activity or efficiency, belonging to the 'Turnover or activity ratios' category. Solvency Ratios, on the other hand, measure a firm's ability to meet its long-term and short-term obligations. Therefore, matching Stock Turnover with Solvency Ratio is incorrect as they belong to different functional classifications.

May/June 2023

129. From the perspective of a shareholder, which two ratios are of primary interest?
(A) Fixed charges cover ratio and Debt service coverage ratio
(B) Quick ratio and Current ratio
(C) Earnings per share and Dividend yield ratio
(D) Stock turnover ratio and Debtors' turnover ratio

Ans :

(C) Earnings per share and Dividend yield ratio
Shareholders, as owners, are primarily concerned with the return on their investment and the value of their shares. Earnings per share (EPS) indicates the profit attributable to each share, driving its value. The Dividend yield ratio shows the direct cash return on the share's current market price. Both are crucial for shareholder analysis.

Oct/Nov 2018

130. A company has the following figures: Current Assets ₹2,00,000; Inventory ₹40,000; Prepaid Expenses ₹10,000; Current Liabilities ₹1,00,000. What is the company's Liquidity Ratio (Quick Ratio)?
(A) 1.5:1
(B) 2:1
(C) 1.6:1
(D) 2.5:1

Ans :

(A) 1.5:1
The Liquidity Ratio is calculated as

$$\frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

Liquid Assets are Current Assets minus Inventory and Prepaid Expenses.
Liquid Assets = ₹ 2,00,000 - ₹ 40,000 - ₹ 10,000 = ₹ 1,50,000 .
Current Liabilities = ₹1,00,000.

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original amount, unlike compound interest where the base for calculation changes over time.

Oct/Nov 2011

4. How is the 'Rate' component in the simple interest formula typically expressed for calculation?

(A) As a whole number integer representing the nominal annual percentage, such as 8 for 8 %.

(B) As a standardized monthly percentage rate, irrespective of the loan's actual tenure.

(C) As a fixed monetary value, such as a specific currency amount, agreed upon by both parties.

(D) As a decimal fraction, which is derived by dividing the annual percentage rate by 100.

Ans :

(D) As a decimal fraction, which is derived by dividing the annual percentage rate by 100.

In the simple interest formula, the 'Rate' is the annual percentage of the principal. For accurate calculation, this percentage must be converted into a decimal fraction. This is achieved by dividing the percentage value by 100. For instance, a rate of 15 % per annum is used as 0.15 in the formula.

May/June 2025

5. In the formula for simple interest, what does the variable 'Time' represent?

(A) The number of compounding periods in a year.

(B) The duration of the loan or deposit expressed in months.

(C) The time in years of the loan or deposit.

(D) The frequency at which interest payments are made.

Ans :

(C) The time in years of the loan or deposit.

The 'Time' variable in the standard simple interest formula, $I = P \times R \times T$, specifically denotes the tenure of the loan or deposit in years. If the time is given in months or days, it must be converted into a fraction of a year to ensure consistency with the annual interest rate.

Oct/Nov 2016

6. A student purchases a computer costing ₹60,000 by taking a loan at a simple interest rate of 12 % per annum. If the loan is to be repaid in a single payment after two years, what will be the total amount paid back?

(A) ₹72,000

(B) ₹74,400

(C) ₹14,400

(D) ₹67,200

Ans :

(B) ₹74,400

First, calculate the total simple interest for two years using the formula

$$I = P \times R \times T.$$

The interest is

₹60,000 × 0.12 × 2 = ₹14,400.

The total amount to be paid back is the sum of the principal and the interest, which is ₹60,000 + ₹14,400 = ₹74,400.

May/June 2012

7. Which of the following formulas correctly represents the accumulated amount (A) at the end of a period under simple interest?

(A) A = P(1 - rt)

(B) $A = P \times r \times t$

(C) A = P + (P/rt)

(D) A = P(1 + rt)

Ans :

(D) A = P(1 + rt)

The accumulated amount (A) is the sum of the initial principal (P) and the total simple interest (I). Since $I = P \times r \times t$, we can write A = P + Prt. By factoring out the principal (P), the formula is simplified to A = P(1 + rt), which represents the final value of a deposit or loan.

Oct/Nov 2005

8. Mohan invests ₹5,000 in a company's fixed deposit that offers a simple interest rate of 9.8 % per annum. How much total interest will he earn at the end of 2 years?

(A) ₹980

(B) ₹490

(C) ₹5,980

(D) ₹1,000

Ans :

(A) ₹980

The simple interest is calculated using the formula $I = P \times r \times t$. Here, the principal (P) is ₹5,000, the annual interest rate (r) is 9.8 % or 0.098, and the time (t) is 2 years.

Therefore, the interest earned is

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₹5,000 ×0.098 × 2 = ₹980.

May/June 2014

9. Jehangir deposits ₹50,000 in a short-term deposit for 180 days at a simple interest rate of 5.3 % per annum. Assuming a 365-day year, what will be the approximate accumulated amount he receives after 180 days?
(A) ₹52,650
(B) ₹50,654
(C) ₹51,307
(D) ₹51,325

Ans :

(C) ₹51,307
To calculate the accumulated amount (A), use the formula A = P(1 + rt). Here, P = ₹50,000, r = 0.053, and t = 180/365 years. The calculation is

$$A = 50{,}000 \times [1 + (0.053 \times 180/365)]$$

Which simplifies to ₹50,000 × 1.02614, resulting in an approximate amount of ₹51,307.

Oct/Nov 2021

10. What fundamental difference distinguishes compound interest from simple interest?
(A) Interest is reinvested to earn further interest, a process not present in simple interest.
(B) Compound interest is exclusively applicable to long-term loans, whereas simple interest is used only for short-term deposits.
(C) Simple interest is always calculated on a daily basis, while compound interest must be calculated on an annual basis.
(D) The nominal rate quoted for a compound interest product is contractually required to be higher than for a simple interest product.

Ans :

(A) Interest is reinvested to earn further interest, a process not present in simple interest.
The core concept of compound interest is that interest is paid not only on the initial principal but also on the accumulated interest from previous periods. This process of "interest on interest" leads to faster growth of the investment or debt compared to simple interest, where interest is calculated only on the original principal amount.

May/June 2021

11. What is the standard formula for the accumulated amount (A) after 'n' years when interest is compounded annually at a rate 'r'?
(A) A = P(1 + nr)
(B) $A = P + (Pr)^n$
(C) $A = P(1 + r/n)$
(D) $A = P(1 + r)^n$

Ans :

(D) $A = P(1 + r)^n$
When interest is compounded annually, the interest earned each year is added to the principal for the next year's calculation. This geometric progression is captured by the formula $A = P(1 + r)^n$, where P is the principal, r is the annual interest rate as a decimal, and n is the number of years.

Oct/Nov 2008

12. If an amount is compounded quarterly, how is the accumulated amount (A) at the end of one year calculated?
(A) $A = P(1 + r)^4$
(B) $A = P(1 + r/4)^4$
(C) $A = P(1 + 4r)$
(D) $A = P(1 + r/12)^{12}$

Ans :

(B) $A = P(1 + r/4)^4$
For quarterly compounding, the annual interest rate (r) is divided by 4 to get the rate per quarter, and the number of compounding periods in one year is 4. Therefore, the formula for the accumulated amount after one year is $A = P(1 + r/4)^4$, reflecting the four compounding cycles within the year.

May/June 2006

13. What is the general formula for compound interest, where 'n' is the number of times interest is compounded per year and 't' is the number of years?
(A) $A = P(1 + r/t)^{nt}$
(B) $A = P(1 + r)^{nt}$
(C) $A = P(1 + r/n)^{nt}$
(D) $A = P(1 + rn)^t$

Ans :

(C) $A = P(1 + r/n)^{nt}$
The general formula for compound interest is $A = P(1 + r/n)^{nt}$. In this formula, 'r' is the annual interest rate, 'n' is the number of compounding periods per year, and 't' is the total number of years. This formula correctly adjusts the rate and the number of periods for any compounding frequency.

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Oct/Nov 2013

14. Based on the data provided in TABLE for an initial principal of ₹10,000 at a 6 % interest rate for one year, which statement is true?

n (compounding)	A (Amount)
1 (yearly)	10,600
2 (semiannually)	10,609
4 (quarterly)	10,613
12 (monthly)	10,616
52 (weekly)	10,618

(A) The accumulated amount decreases as the frequency of compounding increases.
(B) Monthly compounding yields a lower return than semiannual compounding.
(C) The greatest increase in interest earned occurs when moving from yearly to semiannual compounding.
(D) Increasing the number of compounding periods per year leads to a higher accumulated amount.

Ans :

(D) Increasing the number of compounding periods per year leads to a higher accumulated amount.
The table clearly demonstrates a positive correlation between the frequency of compounding (n) and the final accumulated amount (A). As 'n' increases from 1 (yearly) to 52 (weekly), the accumulated amount grows from ₹10,600 to ₹10,618. This illustrates that more frequent compounding results in earning more interest over the same period.

May/June 2015

15. What is the compounding period?
(A) The time interval between which interest is calculated and added to the account balance.
(B) The total duration for which a loan is taken.
(C) The date on which the final loan repayment is due.
(D) The one-year period for which the annual interest rate is quoted.

Ans :

(A) The time interval between which interest is calculated and added to the account balance.
The compounding period is the specific duration after which accrued interest is calculated and capitalized, meaning it is added to the principal. This new, larger principal then earns interest in the subsequent period. Common compounding periods include annually, semi-annually, quarterly, monthly, or even daily, defining the frequency of the compounding effect.

Oct/Nov 2012

16. What mathematical constant is used in the formula for continuously compounded interest?
(A) Pi ($\pi \approx 3.14159$)
(B) The exponential number ($e \approx 2.71828$)
(C) The golden ratio ($\phi \approx 1.61803$)
(D) Avogadro's number ($N_A \approx 6.022 \times 10^{23}$)

Ans :

(B) The exponential number ($e \approx 2.71828$)
When the number of compounding periods 'n' approaches infinity, it is known as continuous compounding. The formula for this scenario is $A = Pe^{rt}$, where 'e' is the base of the natural logarithm, also known as the exponential number. Its approximate value is 2.71828, and it is fundamental to modeling continuous growth.

May/June 2011

17. What does the 'Rule of 72' help to determine?
(A) The exact future value of an investment with monthly compounding.
(B) The approximate number of years it takes for an investment to double with yearly compounding.
(C) The precise interest rate required to achieve a financial goal.
(D) The total interest earned on a loan over its entire tenure.

Ans :

(B) The approximate number of years it takes for an investment to double with yearly compounding.
The Rule of 72 is a simple financial heuristic used to estimate the time required for an investment to double in value at a fixed annual rate of interest. By dividing 72 by the annual percentage rate, one can quickly get an approximation of the doubling time in years, assuming annual compounding.

Oct/Nov 2020

18. Using the Rule of 72, approximately how many years would it take for a debt of ₹1,000 to double to ₹2,000 if the interest rate is 6 % per annum, compounded yearly?
(A) 12 years

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primary feature distinguishing it from a floating rate loan.

Oct/Nov 2019

28. How is the interest rate determined for a floating rate loan?

(A) It is linked to a benchmark rate, such as the MCLR or base rate, and changes as the benchmark changes.

(B) It is fixed at the beginning and remains the same for the entire loan period.

(C) It is negotiated annually between the borrower and the lender.

(D) It is determined by the borrower's credit score at the time of each installment payment.

Ans :

(A) It is linked to a benchmark rate, such as the MCLR or base rate, and changes as the benchmark changes.

A floating or variable interest rate is not fixed. Instead, it is tied to an external benchmark rate set by the bank or the industry, like the Marginal Cost of Funds based Lending Rate (MCLR). As this benchmark rate fluctuates with market conditions, the interest rate on the loan is adjusted accordingly, either increasing or decreasing.

May/June 2009

29. If a home loan is taken at a floating rate of 12 % in April 2021 and the benchmark rate increases, causing the loan rate to become 12.5% in April 2022, what is a likely option for the borrower?

(A) The loan is automatically converted to a fixed rate loan.

(B) The equated monthly instalment (EMI) decreases to compensate for the higher rate.

(C) The repayment period remains the same, but the borrower has to pay a higher EMI.

(D) The loan tenure is automatically foreclosed by the bank.

Ans :

(C) The repayment period remains the same, but the borrower has to pay a higher EMI.

When the interest rate on a floating rate loan increases, the borrower has options. While the default option might be to extend the loan tenure while keeping the EMI constant, the borrower can also choose to pay a higher EMI to keep the original repayment period unchanged. This prevents the loan from extending over a longer duration.

Oct/Nov 2011

30. What is meant by 'front-end interest'?

(A) Interest that is calculated for the tenure and deducted from the principal amount before disbursement.

(B) Interest that is calculated and paid at the end of the loan tenure.

(C) Interest that is charged on the outstanding balance on a quarterly basis.

(D) Interest that is applied only to the front half of the loan's repayment schedule.

Ans :

(A) Interest that is calculated for the tenure and deducted from the principal amount before disbursement.

Front-end interest involves calculating the total interest for the loan's tenure upfront and deducting it from the principal amount. The borrower receives the net amount (Principal - Interest). This practice, common in bill discounting, results in a higher effective interest rate because the borrower pays interest on the full principal but receives a lesser amount.

May/June 2010

31. Which of the following is a typical example of a transaction involving front-end interest?

(A) A housing loan with monthly EMIs.

(B) A savings bank account.

(C) A term loan where interest is applied quarterly.

(D) The discounting of a bill of exchange by a bank.

Ans :

(D) The discounting of a bill of exchange by a bank.

Bill discounting is a classic example of front-end interest. The bank calculates the discount (interest) for the period until the bill's maturity and deducts it from the face value of the bill. The net amount is then paid to the customer. This contrasts with back-end interest typical in term loans.

Oct/Nov 2024

32. Why does the application of front-end interest result in a higher effective interest rate for the borrower?

(A) Because the interest is compounded more frequently than in back-end interest loans.

(B) Because interest is charged on the gross loan

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(B) 1,300,000
(C) 1,276,280
(D) 1,215,506

Ans :

(C) 1,276,280
This is a compound growth problem. The future population can be calculated using the compound interest formula $A = P(1 + r)^n$. Here, P = 1,000,000, r = 0.05, and n = 5.
The calculation is

$$1,000,000 \times (1.05)^5$$
$$= 1,000,000 \times 1.27628$$
$$= 1,276,280.$$

Oct/Nov 2016

24. If the current population of a town is 1 million, which has been growing at a compounded rate of 5 % per year, what was the approximate population three years ago?
(A) 950,000
(B) 850,000
(C) 907,029
(D) 863,838

Ans :

(D) 863,838
To find the population in the past, we need to discount the current population. The formula is

$$P_{past} = P_{present}/(1 + r)^n.$$

Here

$P_{present} = 1,000,000$, r = 0.05, and n = 3.
The calculation is
$\frac{1,000,000}{(1.05)^3} = \frac{1,000,000}{1.157625} \approx 863,838.$

May/June 2014

25. Avichal Publishers buys a machine for ₹20,000. If the rate of depreciation is 10 % per annum, what is the book value of the machine after 3 years?
(A) ₹14,000
(B) ₹13,122
(C) ₹14,580
(D) ₹16,200

Ans :

(C) ₹14,580
Depreciation is calculated similarly to compound interest, but with a negative rate.
The formula for depreciated value is

$$V = P(1 - i)^n.$$

Here, P = ₹20,000, i = 0.10, and n = 3.
The calculation is
₹20,000 × (1 - 0.1)³
= ₹20,000 × (0.9)³
= ₹20,000 × 0.729
= ₹14,580.

Oct/Nov 2007

26. In the machine depreciation example, what is the total amount of depreciation over the 3-year period?
(A) ₹6,000
(B) ₹5,420
(C) ₹5,000
(D) ₹4,580

Ans :

(B) ₹5,420
The total depreciation is the difference between the original value of the machine and its book value after 3 years. The original value was ₹20,000 and the book value after 3 years was calculated to be ₹14,580. Therefore, the total depreciation is ₹20,000 - ₹14,580 = ₹5,420.

May/June 2025

27. What is a key characteristic of a fixed interest rate on a loan?
(A) The rate is directly linked to the bank's MCLR and is automatically adjusted every financial quarter.
(B) The rate is guaranteed to be lower than any prevailing floating interest rates offered by the bank.
(C) The borrower retains the right to unilaterally alter the interest rate at any point during the loan period.
(D) The interest rate is set at the start and remains constant for the loan's entire tenure, regardless of market fluctuations.

Ans :

(D) The interest rate is set at the start and remains constant for the loan's entire tenure, regardless of market fluctuations.
A fixed interest rate is, by definition, constant throughout the loan's life. This provides certainty to the borrower regarding the cost of the loan, as the rate will not increase or decrease even if market interest rates change. This stability is a

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The calculation is (426,000 × 0.15) / 365.
This equals 63,900 / 365, which is approximately ₹175.07, rounded to ₹175.10.

May/June 2013

37. In the daily product method for interest calculation, what does the 'Product' for a given day's balance represent?
(A) The closing balance multiplied by the daily interest rate.
(B) The opening balance plus all credits minus all debits for that day.
(C) The total interest accrued up to that day in the interest period.
(D) The closing balance multiplied by the number of days that balance remains unchanged.

Ans :

(D) The closing balance multiplied by the number of days that balance remains unchanged.
The 'product' in this method is a crucial intermediate step. It is calculated by taking the closing balance of the account and multiplying it by the number of consecutive days that this specific balance is maintained without any change. The sum of all such products over the period forms the basis for the final interest calculation.

Oct/Nov 2021

38. Which of the following is the best definition of an annuity?
(A) A series of fixed payments made or received at a specified frequency over a fixed period.
(B) A single lump-sum payment made at a future date.
(C) An investment whose value grows through continuous compounding.
(D) The interest portion of a loan repayment.

Ans :

(A) A series of fixed payments made or received at a specified frequency over a fixed period.
An annuity is defined as a sequence of equal, fixed payments or receipts that occur at regular intervals over a defined period of time. Common examples include monthly rent payments, car loan payments, or periodic coupon payments from a bond. The consistency of the payment amount and frequency are key characteristics.

May/June 2024

39. What is the primary difference between an ordinary annuity and an annuity due?
(A) The interest rate for an annuity due is always higher.
(B) An ordinary annuity has a finite period, while an annuity due is perpetual.
(C) The timing of the payments within each period.
(D) The currency in which the payments are made.

Ans :

(C) The timing of the payments within each period.
The fundamental distinction between an ordinary annuity and an annuity due lies in the payment timing. For an ordinary annuity, payments are made at the end of each period. For an annuity due, payments are made at the beginning of each period. This timing difference significantly affects their present and future value calculations.

Oct/Nov 2008

40. Which of the following is a typical example of an ordinary annuity?
(A) Coupon payments from a straight bond made at the end of every six months.
(B) Monthly rent payments made at the start of each month.
(C) A lease payment due on the first day of the contract.
(D) An initial deposit into a savings account.

Ans :

(A) Coupon payments from a straight bond made at the end of every six months.
Straight bonds typically make coupon payments to bondholders at the end of each specified period (e.g., semi-annually). Since these are fixed payments occurring at regular intervals at the end of the period, they serve as a classic illustration of an ordinary annuity. Rent payments are typically an example of an annuity due.

May/June 2006

41. Which of the following is provided as an illustration of an annuity due?
(A) Repayment of a loan in Equated Monthly Instalments (EMIs).
(B) A final balloon payment to clear a debt.
(C) A bond's coupon payment at the end of a half-year.

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amount, while the borrower only receives the net amount to use.

(C) Because a mandatory and significant processing fee is always bundled with the calculated front-end interest.

(D) Because the nominal interest rate quoted for front-end interest is statutorily higher.

Ans :

(B) Because interest is charged on the gross loan amount, while the borrower only receives the net amount to use.

The effective interest rate is higher with front-end interest because the interest is calculated on the gross principal, but the borrower only gets the net amount (principal minus interest) to use. This discrepancy between the basis of interest calculation and the actual funds received effectively increases the real cost of borrowing.

May/June 2017

33. What is the normal practice for charging interest in the banking industry, such as for a term loan?

(A) Front-end interest, where discount is deducted upfront.

(B) Flat rate interest, where interest is charged on the initial principal throughout the tenure.

(C) Back-end interest, where the full loan is disbursed and interest is charged subsequently.

(D) Zero-interest, with charges applied as a processing fee.

Ans :

(C) Back-end interest, where the full loan is disbursed and interest is charged subsequently.

The standard and most common practice for loans like term loans is to charge back-end interest. This means the bank disburses the full sanctioned loan amount to the borrower. Interest is then calculated on the outstanding balance at periodic intervals (e.g., monthly, quarterly) and applied subsequently as per the agreed terms.

Oct/Nov 2005

34. How is interest typically calculated in deposit and loan accounts like Savings Accounts or Cash Credit accounts in modern banking?

(A) Based on the minimum balance maintained during the month.

(B) Based on the average closing balance for the quarter.

(C) Based on the balance at the beginning of the interest period.

(D) Based on the actual daily balances in the account.

Ans :

(D) Based on the actual daily balances in the account.

The contemporary method for interest calculation, particularly for savings and cash credit accounts, is based on the daily closing balance. The balance at the end of each day is multiplied by the number of days it remains unchanged to get a 'product'. The sum of these products is then used to calculate the interest.

May/June 2020

35. Question 35. What is the formula for calculating interest for a period using the sum of daily products method?

(A) $\text{Interest} = (\text{Sum of products} \times \text{Rate})/365$

(B) $\text{Interest} = \dfrac{\text{Sum of products} \times \text{Number of days}}{\text{Rate} \times 365}$

(C) $\text{Interest} = \text{Sum of products} \times \text{Rate} \times 365$

(D) $\text{Interest} = (\text{Average balance} \times \text{Rate})/365$

Ans :

(A) $\text{Interest} = (\text{Sum of products} \times \text{Rate})/365$

In the product method, interest is calculated by first finding the sum of daily products for the entire interest period. This total sum is then multiplied by the annual interest rate (as a decimal) and divided by the number of days in a year (typically 365) to arrive at the interest amount for that period.

Oct/Nov 2015

36. Consider the following data for a cash credit account for June 2022. The total of the products is given as ₹426,000. If the interest rate is 15 % p.a., what is the interest for the month of June, using the product method and a 365-day year?

(A) ₹5,325.00

(B) ₹175.10

(C) ₹177.53

(D) ₹426.00

Ans :

(B) ₹175.10

The interest is calculated by applying the formula:

$$\text{Interest} = (\text{Total Products} \times \text{Rate})/365$$

With a total product of ₹426,000 and an annual rate of 15 % (or 0.15)

NODIA

Oct/Nov 2012

46. What does the present value (PV) of an ordinary annuity calculate?

(A) The total sum of all future payments without considering interest.

(B) The current worth of a series of equal future payments, discounted at a given interest rate.

(C) The accumulated value of all payments at the end of the annuity period.

(D) The interest earned on the first payment of the annuity series.

Ans :

(B) The current worth of a series of equal future payments, discounted at a given interest rate.

The present value of an ordinary annuity determines the single lump sum amount today that is equivalent to receiving a series of fixed payments in the future. Each future payment is discounted back to its value at present (time 0) using a specified interest rate, and these discounted values are summed up.

May/June 2011

47. Which of the following financial calculations would most likely use the present value of an ordinary annuity formula?

(A) Determining the maturity value of a recurring deposit.

(B) Calculating the total cost of a loan including all interest.

(C) Estimating the future population of a city.

(D) Finding the present value of future coupon payments from a bond.

Ans :

(D) Finding the present value of future coupon payments from a bond.

Bond pricing involves calculating the present value of its future cash flows. These cash flows consist of periodic coupon payments (an ordinary annuity) and the final principal repayment (a lump sum). The PV of an ordinary annuity formula is essential for valuing the stream of coupon payments to determine the bond's fair price today.

Oct/Nov 2020

48. Using the provided illustrations, what is the present value of a ₹1,000 payment to be received at the end of year 3, if the discount rate is 5 % per annum?

(A) ₹863.84

(B) ₹907.03

(C) ₹822.70

(D) ₹952.38

Ans :

(A) ₹863.84

To find the present value of a single future cash flow, we use the formula

$$\mathrm{PV} = \mathrm{FV}/(1+\mathrm{r})^{\mathrm{n}}$$

Here, the future value (FV) is ₹1,000, the rate (r) is 0.05, and the number of periods (n) is 3.

The calculation is

$$\begin{aligned}\mathrm{PV} &= \frac{1000}{(1.05)^3} \\ &= \frac{1000}{1.157625} \\ &\approx 863.84.\end{aligned}$$

May/June 2022

49. What is the correct formula for the present value (PV) of an ordinary annuity?

(A) $\mathrm{PV} = \mathrm{C} \times \left[\frac{(1+r)^n}{r}\right]$

(B) $\mathrm{PV} = \mathrm{C} \times \left[\frac{r}{(1+r)^n - 1}\right]$

(C) $\mathrm{PV} = \mathrm{C} \times \left[\frac{(1+r)^n - 1}{r(1+r)^n}\right]$

(D) $\mathrm{PV} = \mathrm{C} \times (1+r)^{-n}$

Ans :

(C) $\mathrm{PV} = \mathrm{C} \times \left[\frac{(1+r)^n - 1}{r(1+r)^n}\right]$

This formula is the mathematical shortcut for calculating the present value of an ordinary annuity. It discounts the entire stream of future equal payments ('C') back to their collective value at time zero, using the interest rate 'r' and number of periods 'n'. It is also commonly written as

$$\mathrm{PV} = \mathrm{C} \times \left[\frac{1-(1+r)^{-n}}{r}\right].$$

Oct/Nov 2023

50. Using the formula for the PV of an ordinary annuity, calculate the present value of receiving ₹1,000 at the end of each year for 5 years, with a discount rate of 5 %.

(A) ₹4,329.45

(B) ₹5,525.63

(C) ₹5,000.00

(D) ₹4,545.95

Ans :

(A) ₹4,329.45

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(D) Rent payments required at the beginning of each month.

Ans :

(D) Rent payments required at the beginning of each month.
An annuity due involves payments made at the start of each period. Rent is a common real-world example, as tenants are typically required to pay for the upcoming month at its beginning. This contrasts with an ordinary annuity, where payments occur at the period's end.

Oct/Nov 2017

42. What is the purpose of calculating the future value (FV) of an ordinary annuity?
(A) To determine the current worth of a series of future payments.
(B) To find out the total accumulated amount of a series of investments at a future date.
(C) To calculate the initial principal of a loan based on its EMI.
(D) To find the break-even point of an investment project.

Ans :

(B) To find out the total accumulated amount of a series of investments at a future date.
The future value of an ordinary annuity formula is used to determine the total value of a series of equal, periodic payments at a specific point in the future. It accounts for the compounding of each payment over its respective investment duration, providing the total sum one would have in the future.

May/June 2008

43. Assume you invest ₹1,000 at the end of every year for five years at an interest rate of 5 % p.a. What is the future value of the payment made at the end of the fourth year, when measured at the end of the fifth year?
(A) ₹1,000
(B) ₹1,102.50
(C) ₹1,050
(D) ₹1,215.51

Ans :

(C) ₹1,050
The payment of ₹1,000 made at the end of the fourth year will have one full year to earn interest until the end of the fifth year.
The future value of this single payment is calculated as

$$\begin{aligned} FV &= PV(1+i)^n \\ &= 1{,}000 \times (1.05)^1 \\ &= 1{,}050. \end{aligned}$$

Oct/Nov 2013

44. What is the correct formula for the future value (FV) of an ordinary annuity?
(A) $FV = C \times \left[\frac{i(1+i)^n}{(1+i)^n - 1}\right]$
(B) $FV = C \times (1+i)^n$
(C) $FV = C \times \left[\frac{1-(1+i)^{-n}}{i}\right]$
(D) $FV = C \times \left[\frac{(1+i)^n - 1}{i}\right]$

Ans :

(D) $FV = C \times \left[\frac{(1+i)^n - 1}{i}\right]$
The standard formula to calculate the future value of an ordinary annuity provides a shortcut to summing the future values of all individual payments. In this formula, 'C' is the cash flow per period, 'i' is the interest rate per period, and 'n' is the number of periods.

May/June 2015

45. Using the formula for the FV of an ordinary annuity, calculate the future value of receiving ₹1,000 every year for 5 years at a 5 % interest rate.
(A) ₹5,525.63
(B) ₹5,000.00
(C) ₹4,329.48
(D) ₹5,801.92

Ans :

(A) ₹5,525.63
Using the formula

$$FV = C \times \left[\frac{(1+i)^n - 1}{i}\right]$$

With C = 1,000, $i = 0.05$, and n = 5.
The calculation is

$$\begin{aligned} FV &= 1000 \times \left[\frac{(1.05)^5 - 1}{0.05}\right] \\ &= 1000 \times \left[\frac{1.27628 - 1}{0.05}\right] \\ &= 1000 \times \left[\frac{0.27628}{0.05}\right] \\ &= 1000 \times 5.5256 \end{aligned}$$

Which equals ₹5,525.63.

NODIA

(B) 6 years
(C) 10 years
(D) 18 years

Ans :

(A) 12 years
The Rule of 72 provides an estimate of the doubling time for an investment or debt. To find the approximate number of years, divide 72 by the interest rate percentage.
In this case, 72 / 6 = 12.
Therefore, it would take approximately 12 years for the debt to double at a 6 % annual interest rate.

May/June 2022

19. A savings account with ₹500 is earning 4 % interest, compounded yearly. According to the Rule of 72, how long will it take for the account balance to reach ₹1,000, assuming no further deposits are made?
(A) 12 years
(B) 20 years
(C) 18 years
(D) 24 years

Ans :

(C) 18 years
The question asks for the time it takes for the initial deposit of ₹500 to double to ₹1,000. Applying the Rule of 72, we divide 72 by the annual interest rate of 4 %. The calculation is 72 / 4 = 18. Thus, it will take approximately 18 years for the money to double.

Oct/Nov 2010

20. Consider two statements regarding interest calculation:
Statement I : The simple interest on a certain sum for 3 years is ₹1,200.
Statement II : The compound interest on the same sum for 2 years at the same rate is ₹832.
Based on these statements, what is the annual rate of interest?
(A) 8 %
(B) 6 %
(C) 7 %
(D) 9 %

Ans :

(A) 8 %
From Statement I, Simple Interest per year is ₹1,200 / 3 = ₹400. For compound interest, the interest for the first year is also ₹400.
The interest for the second year is
₹832 - ₹400 = ₹432.
The extra ₹32 is the interest on the first year's interest of ₹400.
The rate R is calculated as

$$R = \frac{32}{400} \times 100 = 8\%.$$

May/June 2005

21. Following the previous question, what is the principal amount (P)?
(A) ₹4,000
(B) ₹6,000
(C) ₹8,000
(D) ₹5,000

Ans :

(D) ₹5,000
We know that the simple interest for one year is ₹400 and the rate is 8 % p.a. Using the simple interest formula for one year,

$$I = P \times R \times T$$

We get

$$400 = P \times 0.08 \times 1$$

Solving for P, we find P = 400 / 0.08 = ₹5,000. This is the original principal amount.

Oct/Nov 2022

22. What is the difference between the compound interest and simple interest for 3 years on the principal of ₹5,000 at an 8 % annual rate?
(A) ₹82.56
(B) ₹98.56
(C) ₹104.12
(D) ₹128.00

Ans :

(B) ₹98.56
The simple interest for 3 years is given as ₹1,200.
The compound interest for 3 years is calculated as
CI = P[(1 + R)3 - 1]
= 5000[(1.08)3 - 1]
= 5000[1.259712 - 1]
= ₹1,298.56.
The difference is ₹1,298.56 - ₹1,200 = ₹98.56.

May/June 2018

23. The population of an industrial town is 1 million and is increasing at a rate of 5 % per year. What will be the estimated population five years from now?
(A) 1,250,000

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Using the formula

$$PV = C \times \left[\frac{(1+r)^n - 1}{r(1+r)^n}\right]$$

With C = 1,000, r = 0.05, and n = 5.

This gives

$$PV = 1000 \times \left[\frac{(1.05)^5 - 1}{0.05 \times (1.05)^5}\right]$$

$$= 1000 \times \left[\frac{0.27628}{0.063814}\right]$$

$$\approx 1000 \times 4.3295$$

$$= 4,329.45.$$

May/June 2016

51. When calculating the future value of an annuity due, why is a modification needed to the ordinary annuity formula?

(A) Because interest rates for annuities due are always compounded differently.

(B) Because annuity due payments are typically larger than ordinary annuity payments.

(C) The number of payments in an annuity due is always one less than in an ordinary annuity.

(D) Because each payment in an annuity due is made one period sooner and thus earns interest for one extra period.

Ans :

(D) Because each payment in an annuity due is made one period sooner and thus earns interest for one extra period.

In an annuity due, payments occur at the beginning of each period. Compared to an ordinary annuity where payments are at the end, each payment in an annuity due has one additional period to accumulate interest. This requires an adjustment to the standard formula, typically by multiplying by (1+i).

Oct/Nov 2009

52. What is the formula for the future value (FV) of an annuity due?

(A) $FV\,(\text{AnnuityDue}) = C \times \left[\frac{(1+i)^n - 1}{i}\right]$

(B) $FV\,(\text{AnnuityDue}) = C \times \left[\frac{(1+i)^n - 1}{i}\right] \times (1+i)$

(C) $FV\,(\text{AnnuityDue}) = C \times \left[\frac{(1+i)^n - 1}{i(1+i)}\right]$

(D) $FV\,(\text{AnnuityDue}) = C \times \left[\frac{1-(1+i)^{-n}}{i}\right] \times (1+i)$

Ans :

(B)

$$FV\,(\text{AnnuityDue}) = C \times \left[\frac{(1+i)^n - 1}{i}\right] \times (1+i)$$

The future value of an annuity due is calculated by first finding the FV of an equivalent ordinary annuity and then compounding it for one additional period. This is achieved by multiplying the ordinary annuity FV formula by the factor (1+i), reflecting the extra period of interest earned by each payment.

May/June 2023

53. If ₹1,000 is invested at the beginning of each year for five years at 5 % interest, what would be the future value of this annuity due at the end of the fifth year?

(A) ₹5,525.63

(B) ₹4,329.48

(C) ₹5,801.91

(D) ₹4,545.92

Ans :

(C) ₹5,801.91

Using the annuity due formula

$$FV = C \times \left[\frac{(1+i)^n - 1}{i}\right] \times (1+i)$$

With C = 1,000, i = 0.05, and n = 5

We get

$$FV = 1000 \times 5.52563 \times 1.05$$

$$= 5,801.91$$

This is higher than the ordinary annuity's FV because each payment earns interest for an additional year.

Oct/Nov 2018

54. Why is the present value of an annuity due greater than the present value of a comparable ordinary annuity?

(A) Because the interest rate used for discounting an annuity due is lower.

(B) Because an annuity due has more payment periods.

(C) Because the calculation includes an extra administrative fee.

(D) Because the annuity due payments are discounted for a lesser amount of time.

Ans :

(D) Because the annuity due payments are discounted for a lesser amount of time.

In an annuity due, payments are received at the beginning of each period, one period earlier than

NODIA

Date	EMI	Interest	Balance towards Principal	Loan Out-standing
15.01.2022	–	–	–	1,00,000
15.02.2022	8,885	1,000	7,885	92,115
15.03.2022	8,885	921	7,964	84,151

(A) ₹1,00,000
(B) ₹92,115
(C) ₹84,151
(D) ₹76,108

Ans :

(C) ₹84,151
The table shows the loan amortization schedule. The initial outstanding was ₹1,00,000. After the first EMI payment on 15.02.2022, the outstanding reduced to ₹92,115. The payment on 15.03.2022 further reduced the principal by ₹7,964, leaving a final outstanding loan amount of ₹84,151 as clearly indicated in the corresponding row.

Oct/Nov 2022

64. What is the EMI for a housing loan of ₹10,00,000 at an interest rate of 10.50 % per annum, repayable in 15 years? (Given: Monthly rate r = 0.00875, n = 180)
(A) ₹10,500
(B) ₹9,847
(C) ₹12,125
(D) ₹11,054

Ans :

(D) ₹11,054
The calculation for EMI is shown using the formula

$$\text{EMI} = \text{P} \times \text{r} \times \frac{(1+\text{r})^{\text{n}}}{(1+\text{r})^{\text{n}} - 1}$$

The text provides the inputs and the final result of this complex calculation. For a principal of ₹10,00,000, monthly rate of 0.00875, and 180 installments, the resulting EMI is calculated to be ₹11,054.

May/June 2018

65. A person wishes to borrow ₹5,000 now and ₹4,000 two years from now. Both loans are to be repaid by equal monthly payments over the next five years. If the interest rate is 10 % compounded monthly, what is the first step in finding the monthly payment?
(A) Bring both loan amounts to their combined present value at the start of the repayment period.
(B) Calculate the future value of both loans at the end of the five-year repayment period.
(C) Sum the two loan amounts to get a total principal of ₹9,000.
(D) Calculate separate EMIs for each loan and add them together.

Ans :

(A) Bring both loan amounts to their combined present value at the start of the repayment period. The repayment annuity starts now. To find the single equivalent EMI, we must equate the present value of all borrowings to the present value of all repayments. The ₹5,000 is already at its present value. The ₹4,000 to be borrowed in two years must be discounted back to its present value today.

Oct/Nov 2016

66. What is an amortisation schedule?
(A) A table showing the future value of an investment at different interest rates.
(B) A schedule that shows the progress of debt repayment, breaking down each payment into interest and principal.
(C) A list of benchmark rates used for floating rate loans.
(D) A chart illustrating the Rule of 72 for various principal amounts.

Ans :

(B) A schedule that shows the progress of debt repayment, breaking down each payment into interest and principal.
An amortisation schedule is a detailed table that tracks the repayment of an interest-bearing loan. For each payment made, it shows how much is applied towards the interest accrued for that period and how much is used to reduce the outstanding principal balance, showing the loan balance after every payment.

May/June 2014

67. Refer to the amortisation schedule in TABLE for a ₹22,000 debt. What is the total interest paid over the life of the loan?

Payment Number	Periodic Payment	Payment of Int @ 2.5 %	Principal Repaid
1	5,000	550.00	4,450

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May/June 2019

59. Refer to TABLE which illustrates the repayment of a ₹1,000 loan over 12 months with equal principal payments. What is the total payment made in the third month?

Balance	Principal Payment	Interest Payment	Total Payment
1,000.00	83.33	6.67	90.00
916.67	83.33	6.11	89.44
833.34	83.33	5.56	88.89

(A) ₹90.00
(B) ₹89.44
(C) ₹88.89
(D) ₹88.33

Ans :

(C) ₹88.89
The table provides a detailed break-up of payments. The first month's payment is ₹90.00. The second month's payment is ₹89.44. The row corresponding to the third month shows a principal payment of ₹83.33 and an interest payment of ₹5.56, resulting in a total payment of ₹83.33 + ₹5.56 = ₹88.89.

Oct/Nov 2006

60. What is the primary advantage of an Equated Monthly Installment (EMI) for borrowers like salaried employees?
(A) The repayment amount is the same for each period, which is suitable for stable incomes.
(B) The total interest paid is lower than other repayment methods.
(C) The principal amount is paid off more quickly at the beginning of the loan.
(D) It does not involve any interest payment for the first year.

Ans :

(A) The repayment amount is the same for each period, which is suitable for stable incomes.
The concept of equated installments was developed to provide a fixed, predictable repayment amount for each period. This is particularly suitable for salaried individuals with stable monthly incomes, as it allows for easier budgeting and financial planning compared to methods where the payment amount changes every month.

May/June 2021

61. What is the correct formula to calculate the Equated Monthly Installment (EMI)?
(A) $EMI = P \times r \times n$
(B) $EMI = (P + I) / n$
(C) $EMI = P\left(\frac{r}{(1+r)^n}\right)$
(D) $EMI = (P \times r)\frac{(1+r)^n}{(1+r)^n - 1}$

Ans :

(D) $EMI = (P \times r)\frac{(1+r)^n}{(1+r)^n - 1}$
This is the standard formula used to calculate the EMI. Here, 'P' is the principal loan amount, 'r' is the rate of interest per installment period (e.g., monthly rate), and 'n' is the total number of installments. This formula mathematically derives a fixed payment that covers both interest and principal over the loan tenure.

Oct/Nov 2010

62. For a loan of ₹1,00,000 at an interest rate of 12 % p.a. (1% per month), to be repaid in 12 months, the calculated EMI is ₹8,885. How is the EMI payment composition structured over the loan tenure?
(A) It is tilted towards principal repayment at the start and interest payments at the end.
(B) It is heavily tilted towards interest payments at the start and principal repayments at the end.
(C) The principal and interest components are equal in every installment.
(D) The entire interest is paid first, followed by principal repayments.

Ans :

(B) It is heavily tilted towards interest payments at the start and principal repayments at the end.
In an EMI-based loan, interest is calculated on the outstanding principal. At the beginning, the principal is high, so the interest component of the EMI is large. As the loan is paid down, the outstanding principal decreases, leading to a smaller interest component and a larger principal component in later EMIs.

May/June 2005

63. Using the data from TABLE for a loan of ₹1,00,000 with an EMI of ₹8,885, what is the outstanding loan amount after the payment on 15.03.2022?

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Ans :

(D) To redeem bond issues or to replace worn-out equipment.
Sinking funds are established for long-term financial goals. Common applications include accumulating funds to pay off a large debt (like a bond issue) when it matures, or to save for the replacement of major assets like machinery or equipment at the end of their useful life.

Oct/Nov 2011

72. The problem of determining the size of a sinking fund deposit is an annuity problem where which variable needs to be determined?
(A) The future value (F).
(B) The size of the periodic payment (A).
(C) The number of periods (n).
(D) The interest rate (i).

Ans :

(B) The size of the periodic payment (A).
In a typical sinking fund problem, the future amount needed (F), the interest rate the fund will earn (i), and the time frame (n) are all known. The objective is to calculate the size of the equal periodic deposit (A or C) that must be made to reach the future value target.

May/June 2010

73. If you wish to accumulate ₹17,000 over 5 years to replace your car by making monthly deposits into a fund that earns 12 % interest compounded monthly, what is the required monthly deposit?
(A) ₹283.33
(B) ₹250.00
(C) ₹208.16
(D) ₹315.45

Ans :

(C) ₹208.16
This is a sinking fund problem where we need to find the annuity payment (A). We use the FV of an ordinary annuity formula and solve for A:

$$A = \frac{F}{\left[\frac{(1+i)^n - 1}{i}\right]}$$

Here F = 17,000, i = 0.12/12 = 0.01, and $n = 5 \times 12 = 60$.
The calculation

$$17{,}000 = A \times \left[\frac{(1.01)^{60} - 1}{0.01}\right] \text{ yields}$$

A = ₹208.16.

Oct/Nov 2024

74. An annuity consists of monthly repayments of ₹600 made over 20 years. The interest rate is 14 % compounded monthly. What is the total amount of money repaid over the 20-year period?
(A) ₹48,250.10
(B) ₹7,80,699.45
(C) ₹1,20,000
(D) ₹1,44,000

Ans :

(D) ₹1,44,000
The total amount repaid is simply the monthly payment multiplied by the total number of payments.
The total number of payments is
$20 \text{ years} \times 12 \text{ months/year} = 240$ payments.
Therefore, the total amount repaid is
₹600 × 240 = ₹1,44,000. This calculation does not involve any discounting or compounding.

May/June 2017

75. For the same annuity of ₹600 per month for 20 years at 14 % compounded monthly, what does the value ₹7,80,699.45 represent?
(A) The future value of the annuity.
(B) The present value of the annuity.
(C) The total principal borrowed.
(D) The total interest paid.

Ans :

(A) The future value of the annuity.
The value ₹7,80,699.45 is the result of calculating the future value of the stream of ₹600 payments. It represents the total accumulated amount at the end of the 20-year period if each payment were invested at 14 % compounded monthly. It is calculated using the future value of an ordinary annuity formula.

Oct/Nov 2005

76. How much money will a student owe at graduation if she borrows ₹3,000 at the end of each year for four years of school, with the loan accruing interest at 5 % per annum?
(A) ₹12,000
(B) ₹12,930
(C) ₹13,550
(D) ₹12,600

Ans :

(B) ₹12,930

NODIA

2	5,000	438.75	4,561.25
3	5,000	324.72	4,675.28
4	5,000	207.84	4,792.16
5	3,609.34	88.03	3,521.31
Total	23,609.34	1,609.34	22,000

(A) ₹23,609.34
(B) ₹22,000.00
(C) ₹550.00
(D) ₹1,609.34

Ans :

(D) ₹1,609.34
The amortisation schedule provides totals at the bottom for checking purposes. The 'Total' row shows the sum of all periodic payments, the sum of all interest payments, and the sum of all principal repayments. The column 'Payment of Int @ 2.5 %' clearly sums up to a total of ₹1,609.34.

Oct/Nov 2007

68. In the amortisation schedule shown in Table 21.4, why is the fifth and final payment (₹3,609.34) different from the previous periodic payments of ₹5,000?
(A) It is a smaller amount required to clear the remaining principal plus the interest for the final period.
(B) It includes a penalty for early repayment of the loan.
(C) It is a pre-agreed balloon payment set at the beginning of the loan.
(D) It is an administrative fee charged at the end of the loan tenure.

Ans :

(A) It is a smaller amount required to clear the remaining principal plus the interest for the final period.
The loan is amortised by payments of ₹5,000 "for as long as necessary". After the fourth payment, the outstanding principal is ₹3,521.31. The final payment only needs to cover this remaining principal plus the interest accrued on it for the last quarter ($3521.31 \times 0.025 = 88.03$), totaling ₹3521.31 + ₹88.03 = ₹3609.34.

May/June 2025

69. What is a "bullet" or "balloon" repayment?
(A) A method where interest is paid in small installments and the principal is waived.
(B) A series of small, equal payments made throughout the loan tenure.
(C) A repayment method where the entire loan amount is repaid at the end of the period, often with accumulated interest.
(D) A loan that is repaid by a single payment at the beginning of the contract period.

Ans :

(C) A repayment method where the entire loan amount is repaid at the end of the period, often with accumulated interest.
A bullet or balloon repayment is characterized by the repayment of the entire loan principal in a single, large sum at the end of the loan term. During the term, payments may consist of interest only, or no payments may be made at all, with interest accumulating until the final maturity date.

Oct/Nov 2019

70. What is a sinking fund?
(A) A fund created by making equal periodic deposits to accumulate a specific amount of money by a specified future date.
(B) A fund used by banks to cover losses from non-performing assets.
(C) An emergency fund set aside for unexpected operational expenses.
(D) A type of mutual fund that invests only in government securities.

Ans :

(A) A fund created by making equal periodic deposits to accumulate a specific amount of money by a specified future date.
A sinking fund is a financial tool used to systematically save for a future obligation. It involves setting aside equal amounts of money at regular intervals. These funds are invested to earn interest, helping to accumulate a targeted sum by a future date to meet a specific goal, such as repaying a debt or replacing an asset.

May/June 2009

71. Which of the following is a common use for a sinking fund?
(A) To pay for daily operating costs of a business.
(B) To speculate on short-term market movements.
(C) To provide short-term working capital for a company.
(D) To redeem bond issues or to replace worn-out equipment.

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in an ordinary annuity. Since each cash flow is received sooner, it is discounted over a shorter duration. The less time a future payment is discounted for, the higher its present value will be.

May/June 2007

55. What is the correct formula for the present value (PV) of an annuity due?

(A) $\text{PV}(\text{AnnuityDue}) = \text{C} \times \left[\frac{(1+r)^n - 1}{r(1+r)^n}\right] \times (1+r)$

(B) $\text{PV}(\text{AnnuityDue}) = \text{C} \times \left[\frac{(1+r)^n - 1}{r(1+r)^n}\right]$

(C) $\text{PV}(\text{AnnuityDue}) = \text{C} \times \left[\frac{(1+r)^n - 1}{r}\right] \times (1+r)$

(D) $\text{PV}(\text{AnnuityDue}) = \text{C} \times \left[\frac{(1+r)^n}{r}\right]$

Ans :

(A) $\text{PV}(\text{AnnuityDue}) = \text{C} \times \left[\frac{(1+r)^n - 1}{r(1+r)^n}\right] \times (1+r)$

To find the present value of an annuity due, the formula for the PV of an ordinary annuity is adjusted to account for the earlier payments. This is done by multiplying the entire ordinary annuity PV formula by the factor (1+r), which effectively shifts each payment's valuation one period forward.

Oct/Nov 2025

56. Calculate the present value of an annuity due of ₹1,000 per period for 5 periods at a 5 % interest rate.

(A) ₹4,329.45
(B) ₹4,545.92
(C) ₹5,801.91
(D) ₹5,525.63

Ans :

(B) ₹4,545.92

The PV of an ordinary annuity for this case is ₹4,329.45. To find the PV of the annuity due, we multiply this value by (1+r).

So,

$$\begin{aligned}\text{PV}_{\text{due}} &= 4,329.45 \times (1 + 0.05) \\ &= 4,329.45 \times 1.05 \\ &= 4,545.92\end{aligned}$$

This higher value reflects the earlier receipt of payments.

May/June 2012

57. Which of the following is NOT listed as a common method of debt repayment in the banking industry in India?

(A) Equal periodic installment of principal, plus interest charged on the outstanding balance.
(B) Equated periodic installment (EMI) that covers both principal and interest components.
(C) Principal-only payments for the first half of the tenure, followed by interest-only payments.
(D) A single bullet or balloon repayment of the entire principal at the end of the loan period.

Ans :

(C) Principal-only payments for the first half of the tenure, followed by interest-only payments.

The text outlines three common debt repayment methods: equal principal installments plus interest, equated installments (EMI), and bullet/balloon repayment. A structure involving principal-only payments followed by interest-only payments is not mentioned as one of these standard methods and is not a common practice for regular loans.

Oct/Nov 2014

58. In the debt repayment method involving equal monthly installments of principal plus interest, what happens to the total payment amount over time?

(A) It decreases over the loan tenure.
(B) It remains constant throughout the loan tenure.
(C) It increases over the loan tenure.
(D) It fluctuates based on the bank's base rate.

Ans :

(A) It decreases over the loan tenure.

In this method, the principal portion of the payment is constant. However, the interest is calculated on the declining outstanding balance. As the principal reduces with each payment, the interest component also decreases. Consequently, the total payment (principal + interest) becomes smaller with each successive installment.

NODIA

This is a future value of an ordinary annuity problem.
We use the formula

$$F = A\left[\frac{(1+i)^n - 1}{i}\right]$$

Where A = 3,000, i = 0.05, and n = 4.
The calculation is

$$F = 3{,}000\left[\frac{(1.05)^4 - 1}{0.05}\right]$$
$$= 3{,}000\left[\frac{1.2155 - 1}{0.05}\right]$$
$$= 3{,}000 \times 4.31$$

Which results in ₹12,930.

May/June 2020

77. A construction company needs to buy a new earthmover for ₹3,50,000 in 5 years. If it can earn a return of 12 % per annum on its savings, what annual amount must it save to purchase the earthmover?
(A) ₹70,000
(B) ₹62,450
(C) ₹49,872
(D) ₹55,093

Ans :

(D) ₹55,093
This is a sinking fund problem to find the annual payment (A).
We use the formula

$$A = F \cdot \left[\frac{i}{(1+i)^n - 1}\right]$$

Where F = 3,50,000, i = 0.12, and n = 5. The calculation is

$$A = 3{,}50{,}000\left[\frac{0.12}{(1.12)^5 - 1}\right]$$
$$= 3{,}50{,}000\left[\frac{0.12}{0.76234}\right]$$

Which results in an annual saving requirement of ₹55,093.

Oct/Nov 2015

78. What is the correct Excel function to find the future value (F) of a uniform series of payments?
(A) =FV(Rate, Nper, Pmt, Pv, Type)
(B) =PMT(Rate, Nper, Pv, Fv, Type)
(C) =PV(Rate, Nper, Pmt, Fv, Type)
(D) =NPER(Rate, Pmt, Pv, Fv, Type)

Ans :

(A) =FV(Rate, Nper, Pmt, Pv, Type)
The Excel function for calculating the future value of an annuity is `FV`. Its arguments are `Rate` (interest rate per period), `Nper` (total number of payment periods), `Pmt` (payment made each period), `Pv` (present value, often 0), and `Type` (0 for end of period, 1 for beginning).

May/June 2013

79. In the Excel function `=PMT(Rate, Nper, Pv, Fv, Type)`, what does the function calculate?
(A) The future value of an investment.
(B) The number of periods for an annuity.
(C) The periodic payment for an annuity, such as a loan repayment or a sinking fund deposit.
(D) The present value of a series of payments.

Ans :

(C) The periodic payment for an annuity, such as a loan repayment or a sinking fund deposit.
The `PMT` function in Excel is used to calculate the periodic payment for an annuity. Given the interest rate, number of periods, and either the present value (for a loan) or future value (for a sinking fund), this function determines the fixed payment amount required per period.

Oct/Nov 2021

80. A company plans to set up a sinking fund to purchase a new machine. The replacement cost is ₹52,000, and the salvage value of the old machine in 10 years is ₹4,000. The fund earns 7 % compounded annually. What is the target amount (F) for the sinking fund?
(A) ₹48,000
(B) ₹52,000
(C) ₹4,000
(D) ₹56,000

Ans :

(A) ₹48,000
The purpose of the sinking fund is to provide for the difference between the cost of the new machine and the salvage value of the old one. Therefore, the target future value (F) that the fund needs to accumulate is

$$\text{Replacement Cost} - \text{Salvage Value}$$
$$= 52{,}000 - 4{,}000 = 48{,}000.$$

May/June 2024

81. Following the previous case, what is the annual payment (A) the company must make into the

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based on market conditions and is linked to a benchmark rate such as the bank's MCLR or base rate. The loan's interest rate will increase or decrease directly in response to changes in this benchmark.

Oct/Nov 2020

90. "The Rule of 72: Allows you to determine the approximate number of years before your money doubles with yearly compounding. Here is how to do it; Divide the number 72 by the percentage rate you are paying on your debt (or earning on your investment)."
Question: If an investment earns 5 % interest compounded yearly, what is the approximate time it will take to double, according to the rule described?
(A) 14.4 years
(B) 10.4 years
(C) 18.0 years
(D) 7.2 years

Ans :

(A) 14.4 years
The source clearly instructs to divide the number 72 by the percentage rate to find the approximate doubling time. For an investment earning 5 %, the calculation is 72 / 5 = 14.4. Therefore, it would take approximately 14.4 years for the investment to double in value.

May/June 2022

91. A person borrows ₹25,000 for 8 years. The interest rate is 18 % per annum, compounded monthly. What are the values of 'r' (periodic rate) and 'n' (number of periods) that should be used in the repayment calculation?
(A) r = 0.18, n = 8
(B) r = 0.015, n = 8
(C) r = 0.18, n = 96
(D) r = 0.015, n = 96

Ans :

(D) r = 0.015, n = 96
The interest is compounded monthly, so the annual rate must be converted to a monthly rate. The periodic rate 'r' is 18% / 12 = 1.5% or 0.015. The loan tenure is 8 years, which translates to $8 \times 12 = 96$ monthly periods. Therefore, r = 0.015 and n = 96.

Oct/Nov 2023

92. A debt of ₹22,000 with interest at 10 % p.a. is to be amortised by quarterly payments. What is the interest due at the end of the first quarter?
(A) ₹2,200
(B) ₹550
(C) ₹1,100
(D) ₹275

Ans :

(B) ₹550
The annual interest rate is 10 %, and the payments are quarterly. Therefore, the interest rate per quarter is 10% / 4 = 2.5%. The interest due at the end of the first quarter is calculated on the initial principal: ₹22,000 × 2.5% = ₹22,000 × 0.025 = ₹550.

May/June 2016

93. Following the previous case, if the first quarterly payment is ₹5,000, what is the outstanding principal balance after this payment?
(A) ₹17,000
(B) ₹21,450
(C) ₹17,550
(D) ₹18,100

Ans :

(C) ₹17,550
The first payment of ₹5,000 is first used to pay the interest due for the quarter, which was calculated as ₹550. The remaining amount of the payment is applied to reduce the principal. So, Principal Reduction = ₹5,000 - ₹550 = ₹4,450. The new outstanding principal is ₹22,000 - ₹4,450 = ₹17,550.

Oct/Nov 2009

94. Identify the incorrect pair from the following.
(A) Simple Interest Formula: $I = P \times r \times t$
(B) Compound Interest Formula (Annual): $A = P(1 + r)^n$
(C) Continuous Compounding Formula: $A = Pe^{rt}$
(D) EMI Formula: EMI = P/n + I

Ans :

(D) EMI Formula: EMI = P/n + I
The formula EMI = P/n + I is incorrect. It vaguely resembles the method of equal principal installments plus interest, but it is not the formula for an Equated Monthly Installment (EMI). The correct EMI formula is a more complex

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(C) Statement 1 is correct, but Statement 2 is incorrect.
(D) Statement 1 is incorrect, but Statement 2 is correct.

Ans :

(A) Both Statement 1 and Statement 2 are correct.
Both statements are correct. For present value, annuity due payments are received earlier and are thus discounted less, resulting in a higher PV. For future value, annuity due payments are made earlier and thus have more time to compound, resulting in a higher FV compared to an ordinary annuity.

Oct/Nov 2013

86. **Assertion (A) :** For a loan repaid by EMI, the interest component of the installment is highest at the beginning.
Reason (R) : Interest in an EMI is calculated on the outstanding principal balance, which is at its highest at the start of the loan.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is true; early EMIs are dominated by the interest portion. Reason (R) is also true and correctly explains why this happens. Since the outstanding loan principal is largest at the beginning, the interest calculated on it for the first period is also the largest.

May/June 2015

87. Which of the following is most likely to have a higher interest rate, all other factors being equal?
(A) A floating rate loan.
(B) A loan with front-end interest.
(C) A loan with back-end interest.
(D) A fixed rate loan.

Ans :

(D) A fixed rate loan.
A fixed rate loan is normally offered at a higher rate than a floating rate loan at the time of origination. This premium compensates the lender for taking on the risk that market interest rates might rise during the loan's tenure, while their return remains locked in at the fixed rate.

Oct/Nov 2012

88. Consider the following statements about debt repayment:
1. In a bullet repayment, the entire principal is paid at the end of the term.
2. An EMI consists of a fixed principal portion and a variable interest portion.
3. In a repayment with equal principal installments, the total periodic payment decreases over time.

Which of these statements is/are correct?
(A) 1 only
(B) 1 and 2 only
(C) 1 and 3 only
(D) 1, 2, and 3

Ans :

(C) 1 and 3 only
Statement 1 is correct by definition. Statement 3 is correct because as the principal reduces, the interest component decreases, making the total payment smaller. Statement 2 is incorrect; an EMI is a fixed total payment, where the composition of principal and interest portions varies over time, not the other way around.

May/June 2011

89. "Floating Rate: In the floating rate or variable rate, the rate of interest changes, depending upon the market conditions. Under floating rate, the interest rate is usually linked to a benchmark rate which could be the MCLR/base rate of the bank... It may increase or decrease depending upon the change in the benchmark rate."
Question: According to the excerpt, what is the primary determinant of the interest rate on a floating rate loan?
(A) The borrower's personal credit history.
(B) The initial agreement, which fixes the rate for the loan's life.
(C) The change in a specified benchmark rate like MCLR.
(D) The profitability of the lending bank in a given year.

Ans :

(C) The change in a specified benchmark rate like MCLR.
The provided text explicitly states that for a floating rate loan, the interest rate changes

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sinking fund for 10 years at 7 % p.a.? (Given the factor $\left[\frac{(1.07)^{10}-1}{0.07}\right] \approx 13.82$)
(A) ₹4,800.00
(B) ₹3,762.66
(C) ₹4,000.00
(D) ₹3,473.23

Ans :

(D) ₹3,473.23
We need to find the annual payment (A) for a sinking fund with F = ₹48,000, n = 10, and r = 0.07.
The formula is

$$F = A \times \text{factor}$$

So

$$A = F/\text{factor}$$
$$= 48,000/13.82$$
$$\approx 3,473.23$$

This is the equal payment to be placed at the end of each year.

Oct/Nov 2008

82. Which of the following pairs is correctly matched?
(A) Ordinary Annuity - Rent payments
(B) Floating Rate - Linked to a benchmark rate
(C) Annuity Due - Bond coupon payments
(D) Simple Interest - Interest earns interest

Ans :

(B) Floating Rate - Linked to a benchmark rate
A floating interest rate is not fixed but changes periodically based on movements in an underlying benchmark rate, such as the bank's MCLR. Rent is an example of an annuity due. Bond coupons are an example of an ordinary annuity. Simple interest does not involve interest earning further interest.

May/June 2006

83. Which of the following statements is incorrect regarding the calculation of interest?
(A) In simple interest, the principal remains unchanged throughout the loan period.
(B) More frequent compounding leads to a higher accumulated amount, given the same nominal rate.
(C) Front-end interest results in a lower effective interest rate for the borrower.
(D) The 'Rule of 72' gives an approximation of the time it takes for money to double.

Ans :

(C) Front-end interest results in a lower effective interest rate for the borrower.
Front-end interest application results in a higher, not lower, effective interest rate. This is because the borrower pays interest calculated on the full principal amount but receives a lesser, net amount for use after the interest is deducted upfront. This increases the actual cost of borrowing.

Oct/Nov 2017

84. Match List-I with List-II and select the correct code.
List-I (Concept)
P. Rule of 72
Q. Sinking Fund
R. Annuity Due
S. Amortisation Schedule
List-II (Description)
1. Payments at the beginning of the period.
2. Estimating doubling time of an investment.
3. Breakdown of payment into principal and interest.
4. Accumulating a future sum through periodic deposits.

Code:
(A) P-2, Q-4, R-1, S-3
(B) P-1, Q-3, R-4, S-2
(C) P-2, Q-1, R-3, S-4
(D) P-4, Q-2, R-1, S-3

Ans :

(A) P-2, Q-4, R-1, S-3
The Rule of 72 (P) is used for estimating the doubling time of an investment (2). A Sinking Fund (Q) is created to accumulate a future sum via periodic deposits (4). An Annuity Due (R) involves payments at the beginning of each period (1). An Amortisation Schedule (S) shows the payment breakdown into principal and interest (3).

May/June 2008

85. Consider the following statements:
Statement 1: The present value of an annuity due is always greater than the present value of an otherwise identical ordinary annuity.
Statement 2: The future value of an annuity due is always greater than the future value of an otherwise identical ordinary annuity.
(A) Both Statement 1 and Statement 2 are correct.
(B) Both Statement 1 and Statement 2 are incorrect.

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expression involving the principal, periodic rate, and number of periods to ensure a constant payment amount.

May/June 2023

95. In the context of the variables used in the chapter's formulas, what does 'n' typically represent in an annuity formula versus a compound interest formula with multiple compounding periods per year?

(A) In annuity formulas, 'n' is the total number of payments, while in the general compound interest formula ($A = P(1 + r/n)^{nt}$), 'n' is the compounding frequency per year.

(B) In annuity formulas, 'n' represents the total number of years, whereas in the compound interest formula, it represents the compounding frequency per month.

(C) In both formula types, 'n' consistently represents the total number of payment periods over the entire life of the financial instrument.

(D) In annuity formulas, 'n' is the compounding frequency per year, whereas in the compound interest formula, it represents the total number of years.

Ans :

(A) In annuity formulas, 'n' is the total number of payments, while in the general compound interest formula ($A = P(1 + r/n)^{nt}$), 'n' is the compounding frequency per year.

There is a subtle difference in notation.

In annuity formulas like

$$FV = C \times \left[\frac{(1+i)^n - 1}{i}\right]$$

'n' represents the total number of payments/ periods.

In the general compound interest formula

$$A = P(1 + r/n)^{nt}$$

'n' specifically represents the number of compounding periods per year, while the total number of periods is nt.

Oct/Nov 2018

96. Which statement correctly describes the relationship between the entries in the 'Principal Repaid' column of an amortisation schedule like Table 21.4 (except the final payment)?

(A) The entries decrease by a fixed amount in each period.

(B) The entries are in a geometric progression with a common ratio of (1+i).

(C) The entries are constant throughout the loan tenure.

(D) The entries are in an arithmetic progression with a common difference of 'i'.

Ans :

(B) The entries are in a geometric progression with a common ratio of (1+i).

The text explicitly notes that the entries in the principal repaid column (except the final one) are in the ratio (1+i). For example, 4,561.25 / 4,450.00 = 1.025, and $4{,}675.28/4{,}561.25 \approx 1.025$. This shows they form a geometric progression, with each subsequent principal repayment being (1+i) times the previous one.

May/June 2007

97. Which of the following defines depreciation as it is applied in the chapter?

(A) A method of calculating interest on an asset.

(B) The increase in an asset's value over time.

(C) A fund set up to purchase a new asset.

(D) A reduction in an asset's value, calculated similarly to compound interest but with a negative rate.

Ans :

(D) A reduction in an asset's value, calculated similarly to compound interest but with a negative rate.

The chapter illustrates depreciation using a formula

$$V = P(1 - i)^n$$

Where 'i' is the rate of depreciation. This is mathematically analogous to the compound interest formula but uses subtraction instead of addition within the parenthesis, representing a periodic reduction in value rather than growth.

Oct/Nov 2025

98. Consider the following three statements regarding interest rates:

1. A fixed rate offers the borrower protection against rising market rates.
2. A floating rate is typically higher than a fixed rate at the time of loan origination.
3. A front-end interest application means the borrower receives the full principal amount.

Which of these statements is/are correct?

(A) 1 only

(B) 1 and 2 only

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(C) 2 and 3 only
(D) 1, 2 and 3

Ans :

(A) 1 only
Statement 1 is correct; the fixed rate protects the borrower from rate hikes. Statement 2 is incorrect; floating rates are normally lower than fixed rates initially. Statement 3 is incorrect; with front-end interest, the interest is deducted upfront, so the borrower receives a net amount, not the full principal.

May/June 2012

99. Which of the following scenarios would require calculating a Present Value?
(A) Determining how much a series of annual deposits will be worth in 10 years.
(B) Calculating the total amount repaid on a 20-year mortgage.
(C) Finding the lump sum amount you need to invest today to receive ₹10,000 per year for 5 years.
(D) Estimating the doubling time of an investment using the Rule of 72.

Ans :

(C) Finding the lump sum amount you need to invest today to receive ₹10,000 per year for 5 years.
This scenario involves determining the current worth of a future stream of income (an annuity). This requires discounting the future payments back to today's value, which is the definition of a present value calculation. The other options involve future value, total payment, or estimation, not present value.

Oct/Nov 2014

100. "Annuities are essentially a series of fixed payments required from you or paid to you at a specified frequency over the course of a fixed period. The most common payment frequencies are yearly (once a year), semi-annually (twice a year), quarterly (four times a year), and monthly (once a month)."
Question: Based on the text, which of the following would NOT be classified as an annuity?
(A) A single dividend payment from a stock.
(B) A monthly car payment of ₹15,000 for 5 years.
(C) A quarterly pension payment of ₹50,000.
(D) A semi-annual coupon payment from a government bond.

Ans :

(A) A single dividend payment from a stock.
The defining characteristic of an annuity, according to the source, is a "series of fixed payments" at a "specified frequency." A single, one-time dividend payment does not fit this definition as it is not part of a series of payments occurring at regular intervals. The other options all represent a series of payments.

May/June 2019

101. "In a term loan, the interest is calculated on the actual daily balances in the account during a period and applied at the end of the period. Obviously, the front-end interest application results in effective interest rate being more as the borrower gets less amount for use whereas, the interest is applied on the full amount."
Question: According to the excerpt, why is the effective rate of a front-end interest loan higher?
(A) Because the interest is applied at the end of the period.
(B) Because interest is calculated on daily balances.
(C) Because the borrower pays interest on the full amount but has use of a smaller, net amount.
(D) Because term loans inherently have higher interest rates than other products.

Ans :

(C) Because the borrower pays interest on the full amount but has use of a smaller, net amount.
The text explicitly states the reason for the higher effective interest rate in a front-end application. It highlights the discrepancy where the borrower "gets less amount for use" (the net amount) while the interest calculation is based "on the full amount" (the gross principal), thus increasing the real cost of borrowing.

Oct/Nov 2006

102. A person takes a loan of ₹1,000 from a friend and agrees to repay it on a monthly basis over one year. The repayment method is equal monthly installments of principal (₹83.33) plus interest on the outstanding balance at 8 % p.a. (0.667% per month). What is the interest payment for the first month?
(A) ₹8.00
(B) ₹6.67
(C) ₹6.11

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(D) ₹5.56

Ans :

(B) ₹6.67
For the first month, the interest is calculated on the entire initial principal of ₹1,000.
Using the monthly interest rate of 0.667 %, the interest payment is
₹1,000 × 0.667% = ₹1,000 × 0.00667 = ₹6.67.
This is the interest portion of the first month's total payment.

May/June 2021

103. Following the previous scenario, what is the outstanding principal owed at the end of the first month, after the first payment has been made?
(A) ₹1,000.00
(B) ₹910.00
(C) ₹916.67
(D) ₹993.33

Ans :

(C) ₹916.67
The repayment method involves a fixed principal payment of ₹83.33 each month. After the first payment is made, the initial principal of ₹1,000 is reduced by this amount. The new outstanding principal is ₹1,000 - ₹83.33 = ₹916.67. This new balance will be used to calculate the interest for the second month.

Oct/Nov 2010

104. "The population of an industrial town is increasing by 5 per cent every year. If the present population is 1 million, estimate the population five years hence." The solution provided is $10,00,000(1.05)^5 = 12,76,280$.
Question: What financial concept is being applied to model the population growth?
(A) Simple Interest
(B) Annuity Due
(C) Sinking Fund
(D) Compound Growth

Ans :

(D) Compound Growth
The formula used, $P_{future} = P_{present}(1+g)^n$, is the standard formula for compound growth. Each year's population increase is based on the previous year's new, larger population, not just the original population. This is analogous to compound interest, where interest is earned on both the principal and previously accumulated interest.

May/June 2005

105. "Avichal Publishers buy a machine for ₹20,000. The rate of depreciation is 10 per cent. Find the depreciated value of the machine after 3 years." The solution provided is $20,000(1\text{-}0.1)^3 = ₹14,580$.
Question: The calculation for depreciation shown in the source is mathematically equivalent to:
(A) Calculating compound interest with a negative interest rate.
(B) Calculating the present value of a future sum.
(C) Calculating the future value of an ordinary annuity.
(D) Calculating simple interest over three years.

Ans :

(A) Calculating compound interest with a negative interest rate.
The formula for depreciation, $V = P(1-i)^n$, directly mirrors the structure of the compound interest formula, $A = P(1+r)^n$. The only difference is the use of a subtraction (1-i) instead of an addition (1+i), signifying a periodic decrease (decay) rather than an increase (growth).

Oct/Nov 2022

106. In a loan repaid by EMI, what happens to the principal and interest components of the EMI over time?
(A) Principal component increases, and Interest component increases.
(B) Principal component increases, and Interest component decreases.
(C) Principal component decreases, and Interest component increases.
(D) Principal component decreases, and Interest component decreases.

Ans :

(B) Principal component increases, and Interest component decreases.
As the loan is repaid, the outstanding principal balance reduces. Since interest is calculated on this declining balance, the interest portion of the fixed EMI decreases with each payment. To keep the EMI constant, the portion of the payment allocated to repaying the principal must therefore increase over time.

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May/June 2018

107. Which of the following statements about annuities is correct?
(A) An annuity due has a lower present value than an equivalent ordinary annuity.
(B) An ordinary annuity has a higher future value than an equivalent annuity due.
(C) All annuities must have monthly payments.
(D) The key difference between an annuity due and an ordinary annuity is the timing of payments.

Ans :

(D) The key difference between an annuity due and an ordinary annuity is the timing of payments.
The fundamental distinction is that annuity due payments occur at the beginning of each period, while ordinary annuity payments occur at the end. This timing difference is the primary factor affecting their present and future values. The other statements are incorrect descriptions of their value relationship and characteristics.

Oct/Nov 2016

108. Which repayment method is most suitable for a borrower who prefers a predictable, constant payment amount each month?
(A) Equated Monthly Installment (EMI).
(B) Equal principal installments plus interest.
(C) Bullet/balloon repayment.
(D) Front-end interest deduction.

Ans :

(A) Equated Monthly Installment (EMI).
The Equated Monthly Installment (EMI) method is specifically designed to have a constant repayment amount throughout the loan tenure. This predictability is highly desirable for borrowers, especially those with stable incomes like salaried employees, as it simplifies budgeting and financial management. Other methods involve variable or lump-sum payments.

May/June 2014

109. Consider the following 4 statements:
1. The formula for simple interest is $\mathrm{I} = \mathrm{P} \times \mathrm{r} \times \mathrm{t}$.
2. The formula for the future value of an ordinary annuity is $\mathrm{FV} = \mathrm{C} \times \left[\frac{(1+i)^n - 1}{i}\right]$.
3. The formula for the present value of an annuity due is $\mathrm{PV} = \mathrm{C} \times \left[\frac{(1+r)^n - 1}{r(1+r)^n}\right]$.
4. The Rule of 72 helps estimate the time for an investment to triple.

Which of the statements are correct?
(A) 1, 2, and 3 only
(B) 3 and 4 only
(C) 1 and 2 only
(D) 1, 2, 3, and 4

Ans :

(C) 1 and 2 only
Statement 1 and 2 provide the correct, standard formulas for simple interest and the future value of an ordinary annuity. Statement 3 is incorrect; it shows the formula for the PV of an ordinary annuity, not an annuity due. Statement 4 is incorrect; the Rule of 72 estimates doubling time, not tripling time.

Oct/Nov 2007

110. **Assertion (A) :** Increasing the frequency of compounding from annually to monthly will result in a higher maturity amount for a deposit.
Reason (R) : With more frequent compounding, interest is capitalized more often, and this capitalized interest starts earning interest itself sooner.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is a well-established principle of compound interest, confirmed by Table 21.1. Reason (R) accurately explains the underlying mechanism: more frequent compounding means interest is added to the principal more often, allowing the "interest on interest" effect to begin earlier and occur more frequently, thus accelerating growth.

May/June 2025

111. Match the financial term in List-I with its appropriate example in List-II.
List-I (Term)
P. Back-end Interest

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Q. Annuity Due
R. Ordinary Annuity
S. Front-end Interest

List-II (Example)
1. Bill Discounting
2. Term Loan
3. Rent Payment
4. Bond Coupon

Code:
(A) P-1, Q-4, R-3, S-2
(B) P-2, Q-4, R-1, S-3
(C) P-1, Q-3, R-2, S-4
(D) P-2, Q-3, R-4, S-1

Ans :

(D) P-2, Q-3, R-4, S-1
Back-end interest (P) is typical for a term loan (2). An annuity due (Q) is exemplified by rent payments made at the start of the month (3). An ordinary annuity (R) is represented by bond coupons paid at the end of a period (4). Front-end interest (S) is applied in bill discounting (1).

Oct/Nov 2019

112. Identify the correct statement regarding debt repayment methods.
(A) A bullet repayment involves a series of equal payments covering both principal and interest.
(B) Repayment with equal principal installments results in a declining total monthly outgo.
(C) An EMI is structured such that the principal portion is highest in the first installment.
(D) All debt repayment methods result in the same total interest paid over the loan's life.

Ans :

(B) Repayment with equal principal installments results in a declining total monthly outgo.
In this method, the principal repayment is constant, but interest is calculated on the reducing balance. As the balance decreases, the interest component also decreases. Therefore, the sum of the constant principal and the decreasing interest results in a total payment that declines over the tenure of the loan.

May/June 2009

113. If P is the principal, r is the annual rate, and t is the time in years, the expression P(1 + rt) calculates:
(A) The compound interest earned.
(B) The present value of a future amount.
(C) The accumulated amount under simple interest.
(D) The simple interest earned.

Ans :

(C) The accumulated amount under simple interest.
The term Prt represents the simple interest (I). The expression P + Prt represents the total accumulated amount (A), which is the principal plus the interest. By factoring out P, we get P(1 + rt). This formula directly calculates the final value of a deposit or loan under the simple interest method.

NODIA

Oct/Nov 2011

114. Which of the following is a primary purpose of creating a sinking fund schedule?
(A) To determine the interest rate for a new loan product.
(B) To compare the profitability of different investment options.
(C) To calculate the monthly EMI for a housing loan.
(D) To show how a fund accumulates to a desired amount over time through periodic deposits.

Ans :

(D) To show how a fund accumulates to a desired amount over time through periodic deposits.
A sinking fund schedule is an amortization-style table that tracks the growth of the fund. It shows the beginning balance, the periodic deposit, the interest earned on the balance, and the ending balance for each period, clearly demonstrating the fund's progression towards its future value target.

May/June 2010

115. A loan is advertised with "interest calculated on a monthly reducing basis." What does this mean?
(A) Interest for any given month is calculated on the principal amount that was outstanding after the previous month's payment.
(B) The interest rate itself reduces every month.
(C) The entire interest for the loan is calculated upfront and reduced from the principal.
(D) Simple interest is applied on a monthly basis.

Ans :

(A) Interest for any given month is calculated on the principal amount that was outstanding after the previous month's payment.

CHAPTER 22

Financial Mathematics – Calculation of YTM

Oct/Nov 2018

1. According to the stated objectives of the unit, which of the following topics is a primary focus of study?
   (A) Equity valuation methods
   (B) The impact of change in interest rate on the value of bonds
   (C) The calculation of foreign exchange rates
   (D) The principles of corporate taxation

   Ans :

   (B) The impact of change in interest rate on the value of bonds
   The unit's objectives explicitly mention understanding the impact of changes in interest rates on bond values. This is a core theme, exploring the relationship between market rates and bond prices, which is fundamental to financial mathematics. Other topics like equity valuation or forex rates are not listed as primary objectives for this specific unit.

May/June 2012

2. What is the term for the combination of debt and equity that a business uses to finance its operations?
   (A) Capital structure
   (B) Financial structure
   (C) Asset composition
   (D) Working capital

   Ans :

   (A) Capital structure
   The mix of debt and equity that a firm or company uses to run its operations is referred to as its capital structure. This blend is crucial for optimizing the cost of capital and maximizing firm value. Debt can arise from various sources like bank borrowings, fixed deposits, or bonds, forming a key component of this structure.

Oct/Nov 2024

3. Which characteristic distinguishes debt from other forms of financing?
   (A) The repayment amount depends on the future valuation of the company.
   (B) It grants the holder a share of ownership in the company.
   (C) The amount to be settled is fixed and specific.
   (D) The returns are paid in the form of dividends.

   Ans :

   (C) The amount to be settled is fixed and specific.
   A defining feature of debt is that the amount to be settled is fixed and specific, and its repayment does not depend on any future valuation of the business. This contrasts with equity, where the value and returns can fluctuate significantly based on the company's performance and market perception. Debt instruments have pre-determined repayment schedules.

May/June 2005

4. In India, what are the bonds issued by private sector companies commonly called?
   (A) Treasury bills
   (B) Commercial papers
   (C) Government securities
   (D) Debentures

   Ans :

   (D) Debentures
   While the term 'bond' is used broadly, bonds issued by private sector companies in India are specifically referred to as debentures. These are debt instruments used by corporations to raise long-term capital from the public. Government entities issue bonds, while private companies issue debentures, which serve a similar function of raising debt capital.

Oct/Nov 2010

5. What legal status do bondholders have in relation to the issuing company?
   (A) They are owners of the company.
   (B) They are partners in the firm.
   (C) They are creditors of the firm.
   (D) They are managers of the company.

   Ans :

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Oct/Nov 2015

120. If a loan's repayment is structured as 'interest paid periodically, and principal paid at the end', this is a form of:
(A) Bullet/balloon repayment.
(B) Equated Monthly Installment (EMI).
(C) Amortised loan with equal principal payments.
(D) Sinking fund repayment.

Ans :

(A) Bullet/balloon repayment.
The chapter describes an alternative form of bullet/balloon repayment where "the interest is paid periodically, as and when applied, and the principal amount of the loan is paid at the end of the contract period." This is a common structure for certain types of loans, distinct from a single lump-sum repayment of both principal and accumulated interest.

May/June 2013

121. "When a specified amount of money is needed at a specified future date, it is a good practice to accumulate systematically a fund by means of equal periodic deposits. Such a fund is called a sinking fund."
Question: Based on this definition, what is the primary objective of a sinking fund?
(A) To provide a regular income stream to the investor.
(B) To minimize the tax liability on investment gains.
(C) To pay for the day-to-day expenses of a business.
(D) To achieve a target financial sum at a future point in time.

Ans :

(D) To achieve a target financial sum at a future point in time.
The excerpt clearly defines a sinking fund as a vehicle to "accumulate systematically" a fund to meet a need for a "specified amount of money at a specified future date." This highlights its role as a goal-oriented savings and investment tool designed to meet a future capital requirement, rather than providing income or covering operational costs.

Oct/Nov 2021

122. A person borrows ₹5,000 now and another ₹4,000 two years from now. The loan requires equal monthly repayments for five years starting from today. The interest rate is 10 % compounded monthly. What is the present value of the total amount borrowed?
(A) ₹9,000.00
(B) ₹8,277.64
(C) ₹9,204.50
(D) ₹7,500.00

Ans :

(B) ₹8,277.64
The present value of the first ₹5,000 is ₹5,000 itself as it is borrowed now. The second loan of ₹4,000 is borrowed in 2 years (24 months), so its present value must be calculated by discounting it back to today.
The total present value is
₹5,000 + ₹4,000 / $(1 + 0.10/12)^{24}$
= ₹5,000 + ₹3,277.64 = ₹8,277.64.

May/June 2024

123. Based on the previous case, the present value of the borrowings is ₹8,277.64. This amount must be equal to the present value of the 60 monthly repayments (R). Which formula would be used to solve for R?
(A) The formula for the future value of an ordinary annuity.
(B) The formula for calculating simple interest.
(C) The formula for the present value of an ordinary annuity.
(D) The Rule of 72.

Ans :

(C) The formula for the present value of an ordinary annuity.
The problem equates the present value of the loans (₹8,277.64) to the present value of the repayment annuity. The formula for the present value of an ordinary annuity

$$PV = R \times \left[\frac{1-(1+r)^{-n}}{r}\right]$$

Would be used. Here, PV is known (₹8,277.64), and the unknown variable to be solved for is the monthly payment, R.

Oct/Nov 2008

124. The total interest paid on an amortised loan is the difference between:
(A) The principal borrowed and the first EMI payment.
(B) The future value of the loan and its present value.

NODIA

"Monthly reducing basis" is the principle underlying EMI calculations. It means that interest for a specific month is not based on the original loan amount, but on the reduced principal balance that remains after the principal portion of the previous month's EMI has been deducted. This is the standard for most retail loans.

Oct/Nov 2024

116. Consider the following statements regarding the calculation of interest.

1. Simple interest is always calculated on the original principal amount.
2. In compound interest, interest is calculated on the principal plus accumulated interest.
3. The formula for the amount with simple interest is $A = P(1+rt)$.
4. Increasing the frequency of compounding decreases the effective interest rate.

Which of the above statements are correct?

(A) 1 and 2 only
(B) 1, 2, and 3 only
(C) 2, 3, and 4 only
(D) All four statements are correct

Ans :

(B) 1, 2, and 3 only
Statements 1, 2, and 3 are all correct definitions and formulas related to simple and compound interest. Statement 4 is incorrect; increasing the compounding frequency (e.g., from annual to monthly) increases the impact of compounding and thus increases, not decreases, the effective interest rate and the final accumulated amount.

May/June 2017

117. What distinguishes a 'floating rate' from a 'variable rate'?

(A) A floating rate is linked to an external benchmark, while a variable rate is set at the bank's discretion.
(B) The terms 'floating rate' and 'variable rate' are used interchangeably in the chapter.
(C) A variable rate changes more frequently than a floating rate.
(D) A floating rate applies to deposits, while a variable rate applies to loans.

Ans :

(B) The terms 'floating rate' and 'variable rate' are used interchangeably in the chapter.
The text explicitly states, "Floating Rates also called as variable rates." and "In the floating rate or variable rate, the rate of interest changes...". This indicates that for the purpose of the concepts discussed in this chapter, the two terms are treated as synonymous, both referring to an interest rate that is not fixed.

Oct/Nov 2005

118. The calculation of interest based on the sum of products divided by 365 is most applicable to which type of accounts?

(A) Savings Accounts and Cash Credit Accounts.
(B) Fixed Deposits and Term Loans.
(C) Bond investments and equity portfolios.
(D) Government pension schemes.

Ans :

(A) Savings Accounts and Cash Credit Accounts.
This method is specifically designed for accounts where the balance fluctuates frequently. It was prevalent for loan accounts like Cash Credit and is now also required for Savings Accounts. It accurately captures the interest on the actual funds held in the account on a day-to-day basis, which is not necessary for fixed-balance products.

May/June 2020

119. A key difference in the cash flow timing for an ordinary annuity versus an annuity due is that:

(A) The first cash flow of an annuity due occurs at time 1, while for an ordinary annuity it's at time 0.
(B) The final cash flow of an annuity due occurs one period after the final cash flow of an ordinary annuity.
(C) The first cash flow of an annuity due occurs at time 0, while for an ordinary annuity it's at time 1.
(D) An annuity due has one more cash flow than an ordinary annuity.

Ans :

(C) The first cash flow of an annuity due occurs at time 0, while for an ordinary annuity it's at time 1.
By convention in finance, "time 0" represents the present moment. An annuity due involves payments at the beginning of each period, so the first payment occurs immediately (time 0). An ordinary annuity has payments at the end of each period, so the first payment occurs at the end of the first period (time 1).

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May/June 2015

129. In the Excel function `F = FV(5%, 4, -3000, 0)`, what does the `-3000` represent?
(A) A present value of ₹3,000.
(B) A series of cash inflows of ₹3,000 each.
(C) A periodic payment or cash outflow of ₹3,000.
(D) A future value target of ₹3,000.

Ans :

(C) A periodic payment or cash outflow of ₹3,000.
In Excel's financial functions, the sign convention is important. Negative numbers represent cash outflows (payments), while positive numbers represent cash inflows (receipts). The `-3000` in the `Pmt` argument signifies a periodic payment of ₹3,000 being made by the investor, as in the case of making annual deposits.

Oct/Nov 2012

130. The entire framework of calculating future and present values of annuities is based on what fundamental financial concept?
(A) The time value of money.
(B) The Rule of 72.
(C) The concept of a sinking fund.
(D) The principle of front-end loading.

Ans :

(A) The time value of money.
The time value of money is the core principle that a sum of money is worth more now than the same sum will be at a future date due to its potential earning capacity. All present and future value calculations, including those for annuities, are applications of this concept, using discounting and compounding to value cash flows across different points in time.

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(C) The first interest payment and the last interest payment.
(D) The sum of all periodic payments and the original principal amount.

Ans :

(D) The sum of all periodic payments and the original principal amount.
The total amount paid by the borrower is the sum of all the periodic payments made over the loan's life. This total payment consists of the original principal plus all the interest charged. Therefore, to find the total interest, one must subtract the original principal from the sum of all payments, as shown in Table 21.4.

May/June 2006

125. The expression $(1+r)^n$ is a common factor in many financial formulas. What does it represent?
(A) The present value factor for a single sum.
(B) The future value factor for an annuity.
(C) The future value factor for a single sum.
(D) The present value factor for an annuity.

Ans :

(C) The future value factor for a single sum.
This expression, $(1+r)^n$, represents the factor by which a single sum of money grows over 'n' periods at an interest rate of 'r' per period. It is the core component of compound interest calculation and is used to find the future value of a present amount ($FV = PV \times (1+r)^n$).

Oct/Nov 2017

126. What is the fundamental assumption when using the formula $F = A\left[\frac{(1+i)^n-1}{i}\right]$ to calculate a sinking fund payment?
(A) The payments are made at the beginning of each period.
(B) The deposits (A) are equal and made at the end of each period (ordinary annuity).
(C) The interest rate 'i' changes every year.
(D) The fund is for an unspecified future date.

Ans :

(B) The deposits (A) are equal and made at the end of each period (ordinary annuity).
This formula is the future value of an ordinary annuity. When used for sinking funds, it assumes that equal periodic deposits are made at the end of each period, and these deposits grow with compound interest to reach the future target amount (F). It is an application of an ordinary annuity.

May/June 2008

127. Which of the following correctly identifies a keyword and its relevance as per the chapter?
(A) Keyword: Annuities; Relevance: A method for calculating simple interest on fluctuating balances.
(B) Keyword: Sinking Fund; Relevance: The interest charged on a loan that is deducted from the principal at disbursement.
(C) The Rule of 72; Relevance: A precise formula for calculating the future value of an annuity due.
(D) Keyword: Compounding Period; Relevance: The time interval at which interest is capitalized and added to the principal.

NODIA

Ans :

(D) Keyword: Compounding Period; Relevance: The time interval at which interest is capitalized and added to the principal.
The compounding period is a crucial concept in compound interest. It defines the frequency (e.g., annually, monthly) at which accrued interest is calculated and added to the principal balance, thereby becoming part of the new principal that earns interest in the next period. The other options misrepresent the keywords.

Oct/Nov 2013

128. If an interest rate is quoted as 12 % per annum compounded monthly, what is the periodic interest rate 'i' used in monthly calculations?
(A) 1 % or 0.01
(B) 12 % or 0.12
(C) 0.1 % or 0.001
(D) The rate cannot be determined without the principal amount.

Ans :

(A) 1 % or 0.01
When the compounding frequency is different from the period for which the rate is quoted, the rate must be adjusted. A rate of 12 % per annum compounded monthly means the annual rate is divided by the number of months in a year. Therefore, the periodic (monthly) rate 'i' is 12% / 12 = 1%, or 0.01 for calculations.

(C) They are creditors of the firm.
When individuals or entities purchase bonds, they are lending money to the issuer. Consequently, they do not receive any ownership stake but instead become creditors of the firm. This status entitles them to receive guaranteed interest payments and the principal amount at maturity, and they can take legal recourse if the issuer defaults on these obligations.

May/June 2021

6. What is the primary advantage of debt capital for an issuing firm regarding tax treatment?
(A) Dividend payments are tax-deductible.
(B) Interest payments on debt are tax-deductible.
(C) Capital gains from bonds are tax-exempt for the firm.
(D) All cash flows from debt are exempt from corporate tax.

Ans :

(B) Interest payments on debt are tax-deductible.
Interest payments on debt are considered a business expense and are therefore tax-deductible. This means they are subtracted from the company's total income before calculating the taxable income. This "tax-shield" lowers the after-tax cost of debt for the firm, providing a significant advantage over equity capital, as dividend payments are not tax-deductible.

Oct/Nov 2016

7. What are the two primary components of expected cash flows from a standard bond?
(A) Dividend payments and capital appreciation
(B) Voting rights and ownership dividends
(C) Bonus shares and rights issues
(D) Interest payments and the repayment of principal

Ans :

(D) Interest payments and the repayment of principal
The expected cash flows for a bond investor consist of a series of periodic interest payments, also known as coupon payments, throughout the life of the bond, plus the repayment of the principal amount at the end of the specified period (maturity). These payments are typically fixed and known to the investor from the outset.

May/June 2014

8. In the context of a bond, who is the lender and who is the borrower?
(A) The holder is the creditor, and the issuer is the debtor.
(B) The holder is the borrower, and the issuer is the lender.
(C) Both the holder and the issuer are considered lenders.
(D) The government is the borrower, and the company is the lender.

Ans :

(A) The holder is the creditor, and the issuer is the debtor.
In a bond transaction, the holder of the bond is the individual or entity that has lent money, making them the lender or creditor. The entity that has issued the bond to raise funds is the borrower or debtor. The issuer is obligated to make specified payments to the holder over the term of the bond.

Oct/Nov 2007

9. What is the main difference between bonds and money market instruments like Certificates of Deposit (CDs)?
(A) The credit risk involved
(B) The tax treatment of interest
(C) The length of the term of the instrument
(D) The currency in which they are denominated

Ans :

(C) The length of the term of the instrument
The primary distinction between bonds and money market instruments such as Certificates of Deposit (CDs) or commercial paper lies in their maturity period. Bonds are typically long-term instruments used to finance long-term investments, whereas money market instruments are short-term, with maturities usually less than a year. Both are forms of debt.

May/June 2025

10. What happens to the market price of a bond as it approaches its maturity date?
(A) It will approach the par value.
(B) It will always increase above its par value.
(C) It will always decrease below its par value.
(D) It will become highly volatile and unpredictable.

Ans :

(A) It will approach the par value.

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(D) Interest: ₹60, Periods: 6
For semi-annual payments, the annual interest of ₹120 (12% of ₹1,000) is halved, resulting in a ₹60 payment every six months. The number of years to maturity (3 years) is doubled to reflect the number of semi-annual periods, resulting in a total of 6 periods. The discount rate per period would be 5%.

May/June 2019

42. Using the data from the previous question (₹60 semi-annual interest, 6 periods, 5% periodic required return) and given $PVIFA_{5\%,6} = 5.0746$ and $PVIF_{5\%,6} = 0.746$, calculate the bond's value.
(A) ₹1,000.00
(B) ₹1,050.48
(C) ₹1,049.44
(D) ₹950.52

Ans :

(B) ₹1,050.48
The bond's value is the sum of the present values of its semi-annual interest payments and principal.
The calculation is

$$(60 \times PVIFA) + (1{,}000 \times PVIF)$$

Using the provided factors:

$$(60 \times 5.0746) + (1{,}000 \times 0.746)$$
$$= 304.48 + 746 = 1{,}050.48.$$

Oct/Nov 2006

43. How is the Current Yield on a bond calculated?
(A) Coupon Interest / Face Value
(B) Change in Price / Original Price
(C) Coupon Interest / Current Market Price
(D) Annual Interest / Yield to Maturity

Ans :

(C) Coupon Interest / Current Market Price
The current yield measures the annual return an investor would earn on a bond if it were purchased at its current market price. It is calculated by dividing the annual coupon interest payment by the bond's current market price. This provides a simple snapshot of the bond's return at a specific point in time.

May/June 2021

44. A bond with a face value of ₹1,000 has an 8% coupon rate. If it is currently quoted in the market at ₹800, what is its current yield?
(A) 8%
(B) 9%
(C) 12.5%
(D) 10%

Ans :

(D) 10%
The current yield is calculated as the annual coupon interest divided by the current market price. The annual interest is 8% of ₹1,000, which is ₹80. The current market price is ₹800. Therefore, the current yield is (₹80 / ₹800) = 0.10, or 10%.

Oct/Nov 2010

45. What does the Yield-to-Maturity (YTM) of a bond represent?
(A) The total return an investor earns by purchasing a bond and holding it until maturity.
(B) The rate of return earned if the bond is sold one year before maturity.
(C) The annual coupon payment as a percentage of the bond's face value.
(D) The current market interest rate for newly issued bonds.

Ans :

(A) The total return an investor earns by purchasing a bond and holding it until maturity.
The Yield-to-Maturity (YTM) is the total anticipated rate of return on a bond if the investor purchases it at the current market price and holds it until it matures. It is the internal rate of return (IRR) of the bond's investment, considering all future coupon payments and the principal repayment.

May/June 2005

46. The YTM is the discount rate that equates the present value of a bond's future cash flows to its:
(A) Face value
(B) Current market price
(C) Redemption value
(D) Original issue price

Ans :

(B) Current market price
Mathematically, the Yield-to-Maturity (YTM) is the specific discount rate at which the sum of the present values of all promised future cash flows (coupons and principal) equals the bond's current market price. It is found by solving for the rate 'k_d' in the bond valuation equation where the bond's value is set to its market price.

NODIA

May/June 2017

16. Under the 'Actual/360' day count convention, how is interest for a year calculated?
(A) By using the actual number of days in the year, including leap years.
(B) By using the actual number of days in the period but assuming the year has 360 days.
(C) By assuming every month has 30 days and the year has 360 days.
(D) By assuming the year always has 365 days, regardless of leap years.

Ans :

(B) By using the actual number of days in the period but assuming the year has 360 days.
The 'Actual/360' day count convention involves using the actual number of days in the interest period for the numerator of the calculation, while the denominator is fixed at 360 days for the year. This method is commonly used in certain money markets and affects the total interest accrued over a specific period.

Oct/Nov 2005

17. Which day count convention assumes every month has 30 days for the purpose of interest calculation?
(A) Actual/Actual
(B) 30/360
(C) Actual/365
(D) Actual/360

Ans :

(B) 30/360
The 30/360 day count convention simplifies interest calculations by assuming that each month has exactly 30 days and the year has 360 days. This method standardizes the calculation, removing variations caused by the actual number of days in different months (e.g., 28, 29, 30, or 31 days) and is common in corporate bond markets.

May/June 2020

18. What is a key characteristic of a fixed rate bond?
(A) Its coupon remains constant throughout the life of the bond.
(B) Its coupon payment varies with a benchmark interest rate.
(C) It pays no regular interest throughout its life.
(D) It can be exchanged for a fixed number of equity shares.

Ans :

(A) Its coupon remains constant throughout the life of the bond.
A fixed rate bond is characterized by a coupon rate that is set at the time of issuance and remains unchanged for the entire term of the bond. This provides the investor with a predictable and stable stream of income, regardless of fluctuations in market interest rates during the bond's life.

Oct/Nov 2015

19. A Floating Rate Note (FRN) has a coupon that is:
(A) Fixed at the time of issue and never changes.
(B) Paid only at the time of maturity.
(C) Linked to a reference rate of interest, causing it to vary.
(D) Indexed to the rate of inflation.

Ans :

(C) Linked to a reference rate of interest, causing it to vary.
Floating Rate Notes (FRNs), or floaters, have a variable coupon that is periodically reset based on a pre-determined benchmark or reference rate of interest, such as the Alternate Reference Rate (ARR). This feature means the interest payments adjust to changes in market interest rates, distinguishing them from fixed-rate bonds.

May/June 2013

20. How do zero-coupon bonds provide a return to the investor?
(A) By being issued at a discount to their par value.
(B) By paying a high, variable coupon rate semi-annually.
(C) By offering stock options in the issuing company.
(D) By making monthly interest payments to the bondholder.

Ans :

(A) By being issued at a discount to their par value.
Zero-coupon bonds, or zeros, do not pay any regular interest (coupons) during their life. Instead, they are issued at a significant discount to their par value. The investor's return is the difference between the discounted purchase price and the full principal amount (par value) received at maturity. The interest is effectively rolled up to maturity.

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Oct/Nov 2021

21. What are high-yield bonds, also known as junk bonds?

(A) Bonds issued by highly stable governments with virtually no default risk.

(B) Bonds that can be converted into a fixed number of the issuer's common stock.

(C) Bonds with a coupon rate that adjusts based on a specific inflation index.

(D) Bonds rated below investment grade by credit rating agencies.

Ans :

(D) Bonds rated below investment grade by credit rating agencies.

High-yield bonds, commonly referred to as junk bonds, are debt securities that have been rated below investment grade by major credit rating agencies. These bonds are considered riskier than investment-grade bonds due to a higher probability of default, and therefore, investors expect a higher yield to compensate for this additional risk.

May/June 2024

22. What option does a convertible bond offer to the bondholder?

(A) The right to compel the issuer to redeem the bond prior to its scheduled maturity.

(B) The option to exchange the bond for a set number of the issuer's common stock shares.

(C) The right to receive periodic interest payments that are adjusted based on inflation.

(D) The right granted to the issuer to repay the bond before its official maturity date.

Ans :

(B) The option to exchange the bond for a set number of the issuer's common stock shares.

A convertible bond provides the bondholder with an embedded option to convert the bond into a pre-specified number of common stock shares of the issuing company. This feature offers the potential for capital appreciation if the company's stock price increases, combining features of both debt and equity for the investor.

Oct/Nov 2008

23. In an inflation-indexed bond, what components are adjusted for inflation?

(A) Only the coupon payments.

(B) Only the principal amount.

(C) Both the principal amount and the interest payments.

(D) The maturity date.

Ans :

(C) Both the principal amount and the interest payments.

Inflation-indexed bonds are designed to protect investors from the eroding effects of inflation. In these bonds, both the principal (or par value) and the periodic interest payments are adjusted based on a specified inflation index. This ensures that the real return on the investment is preserved, regardless of the inflation rate.

NODIA

May/June 2006

24. Which of the following is an example of an asset-backed security (ABS)?

(A) Treasury bonds

(B) Perpetual bonds

(C) Convertible bonds

(D) Collateralized Debt Obligations (CDOs)

Ans :

(D) Collateralized Debt Obligations (CDOs)

Asset-backed securities (ABS) are bonds whose payments are backed by underlying cash flows from a pool of other assets. Examples include Mortgage-Backed Securities (MBSs), Collateralized Mortgage Obligations (CMOs), and Collateralized Debt Obligations (CDOs). These instruments securitize various types of debt, such as mortgages, auto loans, or corporate debt, into tradable securities.

Oct/Nov 2017

25. What is the defining characteristic of subordinated bonds in the event of liquidation?

(A) They have a lower repayment priority than the issuer's other bonds.

(B) They have the highest claim on assets in case of company liquidation.

(C) They are repaid before any other senior or secured debt of the issuer.

(D) They are automatically converted into equity shares upon a liquidation event.

Ans :

(A) They have a lower repayment priority than the issuer's other bonds.

Subordinated bonds, or junior debt, have a lower priority (or rank) compared to other, more senior bonds of the same issuer in case of the company's liquidation or bankruptcy. This means that

senior bondholders must be paid in full before subordinated bondholders can receive any repayment, making them a riskier investment.

May/June 2008

26. How do covered bonds differ from asset-backed securities (ABS)?

(A) Covered bonds are primarily backed by equity instruments, while ABS are backed by debt.
(B) The backing assets remain on the balance sheet of the issuing institution.
(C) Covered bonds have a subordinate claim on assets in case of a company's liquidation.
(D) Covered bonds are a type of zero-coupon instrument that do not pay regular interest.

Ans :

(B) The backing assets remain on the balance sheet of the issuing institution.
The key difference between covered bonds and asset-backed securities (ABS) is the treatment of the underlying assets. For covered bonds, the assets (like mortgages or public sector loans) that back the bond remain on the issuer's balance sheet. In contrast, for ABS, the assets are typically moved to a separate special purpose vehicle (SPV).

Oct/Nov 2013

27. What is a unique feature of perpetual bonds?

(A) They have a very short maturity period.
(B) They have no maturity date.
(C) They pay no coupon interest.
(D) They are always issued by governments.

Ans :

(B) They have no maturity date.
Perpetual bonds, also known as perpetuities or 'Perps', are unique because they do not have a maturity date. The issuer pays coupons indefinitely, and there is no obligation to repay the principal amount. These bonds are treated more like an annuity that continues forever, providing a steady stream of interest payments.

May/June 2015

28. What is the main risk associated with bearer bonds?

(A) They carry a significant risk of being lost or stolen.
(B) They are exposed to high interest rate fluctuations.
(C) They have a high probability of issuer default.
(D) They are not transferable in the secondary market.

Ans :

(A) They carry a significant risk of being lost or stolen.
A bearer bond is an official certificate issued without a named holder. The person who physically possesses the certificate can claim its value, making it similar to cash. This anonymity and lack of registration create a significant risk, as the bonds can be easily lost or stolen, with little to no recourse for the original owner.

Oct/Nov 2012

29. A government bond, also known as a Treasury bond, is generally considered to have no:

(A) Interest rate risk
(B) Inflation risk
(C) Default risk
(D) Liquidity risk

Ans :

(C) Default risk
A government bond, or Treasury bond, is issued by a national government. Because governments have the power to tax and print money, these bonds are considered to be free from default risk, meaning there is virtually no chance that the government will fail to make its promised interest and principal payments.

May/June 2011

30. What right does a 'call option' or 'callability' feature grant to the issuer of a bond?

(A) The right to repay the bond before its scheduled maturity date.
(B) The right to convert the bond into equity shares.
(C) The right to extend the maturity date of the bond.
(D) The right to force the holder to sell the bond back to them at market price.

Ans :

(A) The right to repay the bond before its scheduled maturity date.
Callability, or a call option, is an embedded feature that gives the issuer the right, but not the obligation, to repay or 'call' the bond before its stated maturity date. Issuers typically exercise

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(C) No change in price for a given change in YTM.
(D) The price converging to par value more quickly.

Ans :

(B) A greater change in price for a given change in YTM.
Bond valuation theorems highlight that longer-maturity bonds are more sensitive to changes in interest rates. A change in YTM is applied over a longer series of future cash flows (coupons and principal), leading to a greater cumulative effect on the bond's present value, or price, compared to a shorter-maturity bond.

Oct/Nov 2019

53. According to bond valuation theorems, how do bond price movements react to equal-sized increases and decreases in YTM?
(A) The price movements are symmetrical.
(B) The price change is greater for an increase in YTM than for a decrease.
(C) The price movements are not symmetrical.
(D) The price change is only affected by increases in YTM.

Ans :

(C) The price movements are not symmetrical.
Bond valuation theorems explain the concept of bond convexity. For equal-sized changes in YTM, the price movement is asymmetrical. The price increase resulting from a decrease in YTM is greater in magnitude than the price decrease resulting from an equal-sized increase in YTM.

May/June 2009

54. As per bond valuation theorems, for a given change in YTM, how does the coupon rate affect percentage price changes?
(A) High coupon bonds will have larger percentage price changes.
(B) Low coupon bonds will have smaller percentage price changes.
(C) The coupon rate does not affect the percentage price change.
(D) Low coupon bonds will have larger percentage price changes.

Ans :

(D) Low coupon bonds will have larger percentage price changes.
One of the theorems for bond value states that, other things being equal, the percentage price change for a given shift in YTM will be smaller for high-coupon bonds and larger for low-coupon bonds. Low-coupon bonds have more of their total value tied up in the final principal payment, making them more sensitive to discount rate changes.

Oct/Nov 2011

55. According to bond valuation theorems, what is the effect of a change in YTM on bonds with different YTM levels?
(A) It affects bonds with a higher YTM more than it does bonds with a lower YTM.
(B) It affects bonds with a lower YTM more than bonds with a higher YTM.
(C) It affects all bonds equally, regardless of their YTM.
(D) It only affects bonds trading at a discount.

Ans :

(A) It affects bonds with a higher YTM more than it does bonds with a lower YTM.
Bond valuation theorems suggest that a change in YTM has a greater impact on bonds that already have a higher YTM compared to those with a lower YTM. An illustration of this principle shows a larger percentage price decrease for a bond with a higher initial YTM when both yields increase by the same percentage amount.

May/June 2010

56. Consider the following data for a bond with a required rate of return of 13%.

Years to Maturity	Bond Value
7	₹911.53
6	₹919.78
5	₹929.87
1	₹982.35
0	₹1,000.00

What does this data demonstrate?
(A) The bond value decreases as it gets closer to maturity.
(B) The bond value increases towards its par value as maturity approaches.
(C) The bond is trading at a premium which declines over time.
(D) The bond's value is independent of its time to maturity.

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PVIFA stands for Present Value Interest Factor of an Annuity. It represents the present value of a series of equal payments (an annuity) made over a number of periods. In bond valuation, it is used to quickly calculate the total present value of all the future coupon payments, which are a form of an annuity.

Oct/Nov 2018

37. A bond has a par value of ₹1,000, a coupon rate of 12%, and a maturity of 3 years. If the required rate of return (k_d) is 10%, what is the annual interest payment (I)?
(A) ₹100
(B) ₹1,000
(C) ₹1,200
(D) ₹120

Ans :

(D) ₹120
The annual interest payment is calculated by multiplying the bond's par value by its coupon rate. In this case, the par value is ₹1,000 and the coupon rate is 12%. Therefore, the annual interest payable is ₹1,000 × 12% = ₹120. This amount is the periodic cash flow the investor receives.

May/June 2007

38. A bond with a par value of ₹1,000 and a 12% coupon rate has 3 years to maturity. The required rate of return is 10%. Given $PVIFA_{10\%,3} = 2.487$ and $PVIF_{10\%,3} = 0.751$, what is the value of the bond?
(A) ₹1,000.00
(B) ₹1,049.44
(C) ₹950.25
(D) ₹1,120.00

Ans :

(B) ₹1,049.44
The bond's value is the present value of its cash flows. The annual interest is ₹120 (12% of ₹1,000). The value is calculated as

$$(120 \times PVIFA) + (1{,}000 \times PVIF)$$

Using the given factors:

$$(120 \times 2.487) + (1{,}000 \times 0.751)$$

$$= 298.44 + 751 = 1{,}049.44.$$

Oct/Nov 2025

39. When valuing a bond with semi-annual interest payments, how must the number of years to maturity (n) and the discount rate (k_d) be adjusted?
(A) n is halved, and k_d is doubled.
(B) Both n and k_d are doubled.
(C) n is doubled, and k_d is halved.
(D) Both n and k_d are halved.

Ans :

(C) n is doubled, and k_d is halved.
For a bond paying semi-annual interest, the valuation formula is adjusted to reflect the more frequent cash flows. The number of periods becomes twice the number of years (n is multiplied by 2), and the periodic discount rate becomes half the annual rate (k_d is divided by 2) to match the semi-annual coupon periods.

May/June 2012

40. In the formula for valuing a bond with semi-annual interest

$$V_0 = \sum_{t=1}^{2n} \frac{I/2}{(1 + k_d/2)^t} + \frac{F}{(1 + k_d/2)^{2n}}$$

What does '2n' represent?
(A) The total number of semi-annual periods to maturity.
(B) The doubled annual interest payment.
(C) The halved discount rate.
(D) The face value of the bond.

Ans :

(A) The total number of semi-annual periods to maturity.
In the semi-annual bond valuation formula, 'n' represents the number of years to maturity. Since interest is paid twice a year, the total number of coupon payment periods is doubled. Therefore, '2n' represents the total number of semi-annual periods over the entire life of the bond, used for both summing annuities and discounting the principal.

Oct/Nov 2014

41. A 3-year bond with a ₹1,000 par value and a 12% coupon rate pays interest semi-annually. The required rate of return is 10% annually. What are the semi-annual interest payment and the number of periods?
(A) Interest: ₹120, Periods: 3
(B) Interest: ₹120, Periods: 6
(C) Interest: ₹60, Periods: 3
(D) Interest: ₹60, Periods: 6

Ans :

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Regardless of whether a bond is trading at a premium (above par) or a discount (below par) in the secondary market, its market price will converge towards its par value as the maturity date gets closer. At maturity, the bond is redeemed for its par value, so its market price naturally aligns with this redemption amount.

Oct/Nov 2019

11. What is another name for the Face Value of a bond?
(A) Market Value
(B) Redemption Value
(C) Intrinsic Value
(D) Par Value

Ans :

(D) Par Value
The face value of a bond is also known as its par value. This is the amount stated on the face of the bond, representing the principal that the issuer borrows and promises to repay to the bondholder at the end of the specified maturity period. It serves as the basis for calculating coupon payments.

May/June 2009

12. The specific rate of interest that a bond carries is known as the:
(A) Yield to maturity
(B) Coupon rate
(C) Market interest rate
(D) Discount rate

Ans :

(B) Coupon rate
The coupon rate is the specific, fixed rate of interest that the bond issuer agrees to pay the bondholder. This rate is applied to the bond's face value to determine the annual interest payment, also called the coupon. It is distinct from the market interest rate or the bond's yield, which can fluctuate over time.

Oct/Nov 2011

13. What does the 'Maturity' of a bond signify?
(A) The date on which the bond can first be traded.
(B) The time it takes for the bond's market value to equal its face value.
(C) The period for which the bond is issued and after which it must be repaid.
(D) The date of the first interest payment.

Ans :

(C) The period for which the bond is issued and after which it must be repaid.
The maturity of a bond refers to the specified period for which the bond is issued. At the end of this period, on the maturity date, the issuer is obligated to repay the principal amount (face value) to the bondholder. It defines the lifespan of the debt instrument before it is redeemed by the issuer.

May/June 2010

14. What is the term for the value a bondholder receives when the bond is repaid on its maturity date?
(A) Market Value
(B) Intrinsic Value
(C) Book Value
(D) Redemption Value

Ans :

(D) Redemption Value
The redemption value is the amount the bondholder receives from the issuer on the bond's maturity date. While a bond can be redeemed at a premium or discount, it is generally redeemed at its par value. This value represents the final principal repayment that concludes the life of the bond investment for the holder.

Oct/Nov 2024

15. Which of the following statements about the 'Market Value' of a bond is correct?
(A) It is the price at which the bond is bought or sold in the market.
(B) It is always equal to the bond's face value.
(C) It is fixed for the entire life of the bond.
(D) It is determined solely by the issuer of the bond.

Ans :

(A) It is the price at which the bond is bought or sold in the market.
The market value of a bond is its current trading price on a stock exchange or in the secondary market. This price can differ from the par value and redemption value, fluctuating based on changes in market interest rates, credit quality, and other economic factors. It reflects the present value of the bond's future cash flows.

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Oct/Nov 2022

47. A 9-year bond with a ₹1,000 par value and an 8% coupon is priced at ₹850. To find the YTM, one must solve the equation $850 = 80 \times PVIFA_{k_d,9} + 1000 \times PVIF_{k_d,9}$. If trying a 12% rate gives a value of ₹787.24, what does this imply?
(A) The YTM is exactly 12%.
(B) The YTM is less than 12%.
(C) The YTM is greater than 12%.
(D) The YTM cannot be determined.

Ans :

(B) The YTM is less than 12%.
The market price is ₹850. Using a 12% discount rate results in a lower present value of ₹787.24. Since bond prices and discount rates are inversely related, to get a higher price (from ₹787.24 up to ₹850), a lower discount rate must be used. Therefore, the actual YTM must be less than 12%.

May/June 2018

48. In the YTM calculation example, after testing 12% (value ₹787.24) and 10% (value ₹884.72) for a bond priced at ₹850, the YTM is determined to be between 10% and 12%. What is the name of the method used to find the approximate YTM?
(A) Linear interpolation
(B) Logarithmic extrapolation
(C) Geometric progression
(D) Quadratic equation

Ans :

(A) Linear interpolation
When the exact YTM cannot be solved directly, it is common to find two discount rates that produce values just above and just below the bond's market price. Linear interpolation is then used to estimate the rate between these two points that would correspond to the market price, providing an approximate value for the YTM.

Oct/Nov 2016

49. According to bond valuation theorems, if a bond's coupon rate is 8% and the market interest rate is 6%, the bond will trade at:
(A) Par
(B) A discount
(C) A premium
(D) A price unrelated to the interest rate

Ans :

(C) A premium
According to bond valuation theorems, when the required rate of return (6%) is less than the bond's coupon rate (8%), the value of the bond will be greater than its par value. Investors are willing to pay more for a bond that offers a higher coupon than what is currently available in the market.

May/June 2014

50. According to the theorems for bond value, what happens to the price of a bond trading at a discount as it approaches maturity?
(A) The discount on the bond declines.
(B) The discount on the bond increases.
(C) The price of the bond remains constant.
(D) The bond's price falls further below par.

Ans :

(A) The discount on the bond declines.
One of the theorems for bond value states that when the required rate of return is greater than the coupon rate (a discount bond), the discount on the bond declines as maturity approaches. This means the bond's price will gradually increase over its remaining life, converging towards its par value at the maturity date.

Oct/Nov 2007

51. According to the theorems for bond value, what is the relationship between a bond's price and its yield to maturity (YTM)?
(A) They are directly related.
(B) There is no relationship between them.
(C) The relationship is positive for premium bonds and negative for discount bonds.
(D) They are inversely related.

Ans :

(D) They are inversely related.
A fundamental principle of bond valuation is that a bond's price is inversely related to its yield to maturity. This means that as the YTM (market yield) increases, the price of the bond decreases, and conversely, as the YTM decreases, the price of the bond increases.

May/June 2025

52. According to bond valuation theorems, for a given difference between YTM and coupon rate, a longer term to maturity results in:
(A) A smaller change in price for a given change in YTM.
(B) A greater change in price for a given change in YTM.

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this option when interest rates fall, allowing them to refinance their debt at a lower cost.

Oct/Nov 2020

31. What is the premium that an issuer may have to pay when exercising a call option on a bond called?
(A) Put premium
(B) Conversion premium
(C) Liquidity premium
(D) Call premium

Ans :

(D) Call premium
When an issuer calls a bond before its maturity, they may be required to pay an amount greater than the bond's par value. This additional amount paid to the bondholder as compensation for the early redemption is known as the call premium. It serves to make the early redemption more attractive to the investor.

May/June 2022

32. A 'put option' or 'putability' feature in a bond gives a right to the:
(A) Issuer to repay the bond before maturity.
(B) Holder to force the issuer to repay the bond before maturity.
(C) Holder to extend the bond's maturity.
(D) Issuer to convert the bond to stock.

Ans :

(B) Holder to force the issuer to repay the bond before maturity.
Putability, or a put option, is an embedded feature that benefits the bondholder. It grants the holder the right, but not the obligation, to sell the bond back to the issuer at a predetermined price on specified dates before maturity. Holders may exercise this right if interest rates rise, allowing them to reinvest at a higher rate.

Oct/Nov 2023

33. Bonds that contain a put option are also referred to as:
(A) Callable bonds
(B) Convertible bonds
(C) Retractable or putable bonds
(D) Subordinated bonds

Ans :

(C) Retractable or putable bonds
Bonds that include a putability feature, which allows the holder to force an early redemption, are commonly referred to as retractable bonds or putable bonds. This term highlights the holder's ability to 'retract' their investment before the scheduled maturity date, providing a degree of protection against rising interest rates.

May/June 2016

34. The intrinsic value of a bond is defined as the:
(A) Face value printed on the bond certificate.
(B) Price at which it was originally issued.
(C) Average trading price over the last year.
(D) Present value of its future cash streams.

Ans :

(D) Present value of its future cash streams.
The intrinsic value of a bond is its theoretical worth, calculated as the present value of all the future cash flows the bond is expected to generate. This includes all future coupon payments and the final principal repayment, discounted back to the present using an appropriate discount rate, which reflects the required rate of return.

Oct/Nov 2009

35. In the bond valuation formula

$$V_0 = \sum_{t=1}^{n} \frac{I}{(1+k_d)^t} + \frac{F}{(1+k_d)^n}$$

What does the term 'F' represent?
(A) The annual interest payment.
(B) The frequency of coupon payments.
(C) The redeemable value of the bond at maturity.
(D) The cost of capital (k_d).

Ans :

(C) The redeemable value of the bond at maturity.
In the standard bond valuation formula, the variable 'F' represents the future redeemable value of the bond. This is the principal amount, also known as the face value or par value, that the issuer repays to the bondholder at the end of the bond's life, i.e., at maturity.

May/June 2023

36. In bond valuation, what does PVIFA represent?
(A) The present value of a single future sum.
(B) The present value of an ordinary annuity.
(C) The future value of a series of payments.
(D) The interest rate applied to the bond.

Ans :

(B) The present value of an ordinary annuity.

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Ans :

(B) The bond value increases towards its par value as maturity approaches.
The table shows that the bond's value, which is initially below par (₹911.53 < ₹1,000), consistently increases as the years to maturity decrease. The value moves from ₹911.53 with 7 years left to ₹1,000.00 at maturity (0 years left), perfectly illustrating that a discount bond's price converges upward to its par value over time.

Oct/Nov 2024

57. Bond X has a 3-year maturity and Bond Y has a 6-year maturity. Both have a 10% coupon and a ₹1,000 face value. When YTM increases from 10% to 11%, Bond X's price drops by 2.5%, while Bond Y's price drops by 4.2%. What principle does this illustrate?
(A) Bonds with higher coupons are less sensitive to interest rate changes.
(B) Longer-term bonds are more sensitive to interest rate changes than short-term bonds.
(C) Bond prices and YTM are directly related.
(D) All bonds have the same price sensitivity regardless of maturity.

Ans :

(B) Longer-term bonds are more sensitive to interest rate changes than short-term bonds.
This scenario directly illustrates a key bond theorem. Bond Y, with the longer maturity of 6 years, experiences a larger percentage price drop (4.2%) compared to Bond X, with the shorter maturity of 3 years (2.5%), for the same 1% increase in YTM. This demonstrates the greater price sensitivity of longer-term bonds.

May/June 2017

58. A 5-year, 10% coupon bond is initially priced at its par value of ₹1,000 (YTM=10%). A 1% increase in YTM to 11% causes a 3.7% price decrease. A 1% decrease in YTM to 9% causes a 3.9% price increase. What does this demonstrate?
(A) The asymmetrical nature of bond price changes.
(B) The symmetrical nature of bond price changes.
(C) That price changes are always equal to the change in YTM.
(D) That bond prices are not affected by YTM changes.

Ans :

(A) The asymmetrical nature of bond price changes.
This example illustrates that the magnitude of the price increase (3.9%) for a 1% decrease in yield is larger than the magnitude of the price decrease (3.7%) for a 1% increase in yield. This shows that bond price movements are not symmetrical in response to equal-sized changes in YTM in opposite directions, a property known as convexity.

Oct/Nov 2005

59. Bond X (YTM 10%) and Bond Y (YTM 20%) are identical otherwise. A 20% increase in YTM causes Bond X's value to drop by 8%, while Bond Y's value drops by 13%. What bond theorem does this example illustrate?
(A) The inverse relationship between price and yield.
(B) That longer maturity bonds are more sensitive to rate changes.
(C) The effect of the YTM level on price changes.
(D) The asymmetrical nature of bond price movements.

Ans :

(C) The effect of the YTM level on price changes.
This case compares two bonds that differ only by their initial YTM. Bond Y, with the higher initial YTM of 20%, experiences a more significant percentage price decrease (13%) than Bond X, with the lower YTM of 10% (8%). This directly illustrates the principle that a change in YTM has a greater impact on bonds that already have a higher YTM.

May/June 2020

60. What is the underlying assumption regarding periodic interest payments in all aspects of bond valuation and duration?
(A) They are reinvested at the prevailing market rate.
(B) They are immediately spent by the investor.
(C) They are reinvested at the original coupon rate.
(D) They are not reinvested and held as cash.

Ans :

(A) They are reinvested at the prevailing market rate.
A crucial underlying assumption in bond valuation, and particularly in the concept of duration, is that the periodic interest (coupon)

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in YTM is negative. The product of two negative numbers is positive, indicating a price increase.

May/June 2018

90. If the prevailing market interest rate is more than the coupon rate, the existing bond will command a lower value. Why?
(A) Buyers prefer new bonds offering the higher current market coupon.
(B) The bond's underlying credit quality has suddenly and significantly decreased.
(C) The issuing company is now much more likely to default on its promised payments.
(D) The bond's maturity date is approaching too quickly for investors to profit.

Ans :

(A) Buyers prefer new bonds offering the higher current market coupon.
When market interest rates rise above a bond's fixed coupon rate, newly issued bonds offer more attractive yields. A rational investor would prefer to buy a new bond paying the higher market rate. Consequently, to be competitive, the price of the existing, lower-coupon bond must fall to a level where its overall yield matches the new market rate.

Oct/Nov 2016

91. Which of the following is NOT typically listed as a keyword in a chapter on bond valuation?
(A) Face Value
(B) Yield-to-Maturity
(C) Duration of Bond
(D) Equity Premium

Ans :

(D) Equity Premium
A summary of core terminology for a bond chapter would include terms like Face Value, Coupon Rate, Maturity, Redemption Value, Market Value, Intrinsic Value, Yield-to-Maturity, and Duration of Bond. Equity Premium, which relates to the excess return of stocks over a risk-free rate, is a concept from equity valuation, not bond valuation.

May/June 2014

92. Which of the following statements about bonds is incorrect?
(A) Bonds are debt instruments.
(B) Bonds are part of the net worth of an enterprise.
(C) A bond is issued for a specified period of time.
(D) A bond carries a specific rate of interest.

Ans :

(B) Bonds are part of the net worth of an enterprise.
Bonds represent debt or a liability for the issuing enterprise, not ownership equity. Net worth (or equity) consists of share capital and reserves. Therefore, the statement that bonds are part of the net worth is incorrect. Bondholders are creditors, not owners, and their investment is a loan to the company.

Oct/Nov 2007

93. How is the duration of a bond defined in the context of risk management?
(A) The total time remaining until the bond's principal is repaid.
(B) The holding period that neutralizes interest rate risk.
(C) The entire period for which the bond was originally issued to investors.
(D) The time gap between two consecutive semi-annual or annual interest payments.

Ans :

(B) The holding period that neutralizes interest rate risk.
The concept of duration is defined as the specific holding period where the investor is immunized against interest rate risk. At this point, the loss in price due to a rate increase is exactly offset by the gain from reinvesting coupons at that higher rate, and vice versa, thus making the realized yield insensitive to rate changes.

May/June 2025

94. Which statement regarding bond optionality is correct?
(A) Bonds can be issued only with a call option.
(B) Bonds can be issued only with a put option.
(C) Bonds cannot be issued with a put or call option.
(D) Bonds can be issued with both put and call option.

Ans :

(D) Bonds can be issued with both put and call option.
Bonds can be structured with various embedded options. They can be issued with a call option

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calculated as 3.99 years, what does this value signify?

(A) The interest rate risk will disappear if the bond is held for 3.99 years.
(B) The bond will mature in 3.99 years.
(C) The investor must hold the bond for 5 years to avoid risk.
(D) The bond's price will be highest at 3.99 years.

Ans :

(A) The interest rate risk will disappear if the bond is held for 3.99 years.

The calculated duration of 3.99 years indicates the immunization point for this bond. If an investor's holding period matches this duration, their realized yield will be protected from changes in market interest rates. The loss on bond price from a rate increase would be offset by higher reinvestment income, and vice-versa.

May/June 2006

66. How is the duration of an entire portfolio of bonds computed?

(A) It is the simple average of the durations of the individual bonds.
(B) It is the weighted average of the durations of the individual bonds.
(C) It is the duration of the bond with the longest maturity in the portfolio.
(D) It is the duration of the bond with the highest coupon rate.

Ans :

(B) It is the weighted average of the durations of the individual bonds.

The duration of a bond portfolio is not a simple average. It is calculated as the weighted average of the durations of the individual bonds that make up the portfolio. The weight of each bond is typically its market value as a proportion of the total market value of the portfolio.

Oct/Nov 2017

67. How is Modified Duration calculated from Macaulay Duration?

(A) Modified Duration $=$ Duration $\times (1 + k_d)$
(B) Modified Duration $=$ Duration $- (1 + k_d)$
(C) Modified Duration $=$ Duration $+ k_d$
(D) Modified Duration $= \dfrac{\text{Duration}}{1 + k_d}$

Ans :

(D) ModifiedDuration $= \dfrac{\text{Duration}}{1 + k_d}$

Modified Duration is derived directly from Macaulay Duration. It is calculated by dividing the Macaulay Duration by the factor$(1 + k_d)$, where 'k_d' is the Yield-to-Maturity (YTM) of the bond per period, expressed as a fraction. Modified Duration provides a direct measure of percentage price volatility.

May/June 2008

68. If the Macaulay Duration of a bond is 6.9 years and its YTM is 10%, what is its Modified Duration?

(A) 6.27 years
(B) 7.59 years
(C) 6.9 years
(D) 0.69 years

Ans :

(A) 6.27 years

Modified Duration is calculated as

$$\frac{\text{Macaulay Duration}}{1 + \text{YTM}}$$

Given a Macaulay Duration of 6.9 years and a YTM of 10% (or 0.10), the calculation is

$$\frac{6.9}{1 + 0.10} = \frac{6.9}{1.1} = 6.27 \text{ years.}$$

This value can be used to estimate the bond's price change for a 1% change in yield.

NODIA

Oct/Nov 2013

69. Based on the properties of duration, which of the following bonds would have the longest duration, assuming all have the same maturity and yield?

(A) A 10% coupon bond
(B) A 8% coupon bond
(C) A zero-coupon bond
(D) A 6% coupon bond

Ans :

(C) A zero-coupon bond

According to the properties of duration, a zero-coupon bond's duration is equal to its maturity, while coupon-paying bonds have durations less than their maturity. Furthermore, a larger coupon rate leads to a smaller duration. Therefore, the zero-coupon bond, which pays its entire cash flow at maturity, will have the longest duration among the choices.

May/June 2015

70. What is the duration of a perpetual bond, where 'r' is the current yield?

is the 8% coupon on ₹1,00,000 (which is ₹8,000) plus the ₹1,00,000 face value, totaling ₹1,08,000.

May/June 2007

80. For Company A's bond, the Macaulay Duration is calculated to be 4.34 years and the YTM is 6%. What is the Modified Duration (MD) of this bond?
(A) 4.10 years
(B) 4.60 years
(C) 4.34 years
(D) 4.00 years

Ans :

(A) 4.10 years
Modified Duration is calculated by dividing the Macaulay Duration by $(1 + \text{YTM})$.
Given a Macaulay Duration of 4.34 years and a YTM of 6% (or 0.06), the Modified Duration is
$\frac{4.34}{1+0.06} = \frac{4.34}{1.06} \approx 4.10$ years.
This figure is a direct measure of the bond's price sensitivity.

Oct/Nov 2025

81. Using the calculated Modified Duration of 4.10 for Company A's bond, what is the expected percentage change in the bond's price if the YTM falls by 100 basis points (1%)?
(A) A decrease of 4.1%
(B) An increase of 0.41%
(C) A decrease of 0.41%
(D) An increase of 4.1%

Ans :

(D) An increase of 4.1%
The percentage change in price is estimated by: $-\text{MD} \times (\text{change in YTM})$. Here, $\text{MD} = 4.10$ and the change in YTM is a fall of 1%, or -0.01. So, the price change is $-4.10 \times (-0.01) = +0.041$, or a 4.1% increase. This is consistent with the inverse relationship between price and yield.

May/June 2012

82. Consider two bonds, A and B, with the following characteristics:

Particulars	Bond A	Bond B
Face value	₹100	₹100
Coupon rate	14%	14%
Current market price	₹100	₹100
Term to maturity	4 yrs	7 yrs

What is the YTM for both Bond A and Bond B?
(A) 10%
(B) 14%
(C) 12%
(D) Cannot be determined

Ans :

(B) 14%
According to bond valuation principles, when a bond's current market price is equal to its face value, its Yield-to-Maturity (YTM) must be equal to its coupon rate. Since both Bond A and Bond B are trading at their face value of ₹100, their YTM is equal to their coupon rate of 14%.

Oct/Nov 2014

83. Following up on Bond A (4-yr, 14% coupon) and Bond B (7-yr, 14% coupon), if interest rates fall by 1%, the YTM for both becomes 13%. Bond A's price increases to ₹102.94 (a 2.94% change), and Bond B's price increases to ₹104.42 (a 4.42% change). What conclusion can be drawn?
(A) Shorter-term bonds experience greater price changes.
(B) All bonds experience the same percentage price change.
(C) Longer-term bonds experience greater price changes for the same yield change.
(D) Price changes are independent of the term to maturity.

Ans :

(C) Longer-term bonds experience greater price changes for the same yield change.
The case shows that for the same 1% decrease in YTM, Bond B (7-year maturity) had a larger price increase (4.42%) than Bond A (4-year maturity), which saw a 2.94% increase. This demonstrates that bonds with a longer term to maturity are more sensitive to changes in interest rates.

May/June 2019

84. For Bond A (4-yr, 14% coupon), a 1% fall in interest rates caused a 2.94% price increase. A 1% rise in interest rates caused a 2.83% price decrease. This observation confirms that the percentage price change in a bond is:
(A) Symmetrical
(B) Always positive
(C) Always equal to the change in interest rate
(D) Asymmetrical

Ans :

(D) Asymmetrical

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(C) Interest rate elasticity is independent of duration.
(D) Interest rate elasticity is always equal to -1.

Ans :

(A) Duration and interest rate elasticity are directly related.
The formula shows a direct link between Modified Duration and Interest Rate Elasticity. A higher duration leads to a higher (in absolute terms) interest rate elasticity. Therefore, anything that causes a bond's duration to increase, such as a longer maturity or lower coupon, will also increase its interest rate elasticity and price volatility.

May/June 2016

76. A 10-year bond with a ₹1,000 face value and a 10% coupon rate is priced at ₹1,000. When the market rate changes to 11%, the price drops to ₹940.90. What is the percentage change in price?
(A) -10.00%
(B) -5.91%
(C) -11.00%
(D) +5.91%

Ans :

(B) -5.91%
The percentage change in price is calculated as

$$\frac{\text{New Price} - \text{Old Price}}{\text{Old Price}}$$

Here, the price changes from ₹1,000 to ₹940.90.
The change is ₹940.90 - ₹1,000 = -₹59.10.
The percentage change is

$$\left(\frac{-59.10}{1,000}\right) \times 100 = -5.91\%.$$

Oct/Nov 2009

77. The Interest Rate Elasticity (IE) for the bond in the previous question is calculated as -5.91%. The change in YTM was from 10% to 11%, which is a 10% relative change in yield ($\frac{11-10}{10}$). If the calculation yields an IE of 5.91 per cent, what is it likely referring to?
(A) The percentage price change for a 1% absolute change in yield.
(B) The percentage price change for a 10% relative change in yield.
(C) The Modified Duration of the bond.
(D) The Macaulay Duration of the bond.

Ans :

(B) The percentage price change for a 10% relative change in yield.
The text calculates IE as

$$\frac{(-59.10/1,000) \times 100}{10\%} = 5.91 \text{ percent.}$$

The denominator of 10% here represents the percentage change in YTM, not the absolute change. It implies a 10% change in YTM would cause a 5.91% change in price in the opposite direction.

May/June 2023

78. A bond from Company A has a face value of ₹1,00,000, a coupon rate of 8%, a YTM of 6%, and 5 years to maturity. The total present value of its cash flows is calculated to be ₹1,08,424.72. What can be concluded from this value?
(A) The bond is trading at a premium.
(B) The bond is trading at a discount.
(C) The YTM is higher than the coupon rate.
(D) The bond's market price is equal to its face value.

Ans :

(A) The bond is trading at a premium.
The bond's present value (market price) is ₹1,08,424.72, which is greater than its face value of ₹1,00,000. This indicates the bond is trading at a premium. This is consistent with bond valuation theory, as the YTM (6%) is lower than the coupon rate (8%), making the bond more attractive to investors.

Oct/Nov 2018

79. In a duration calculation table for Company A's bond, the final cash flow at Year 5 is ₹1,08,000. What does this amount represent?
(A) The single annual interest (coupon) payment for that year.
(B) The total undiscounted sum of all coupon payments over the bond's life.
(C) The final coupon payment plus the principal repayment.
(D) The projected market selling price of the bond in Year 5.

Ans :

(C) The final coupon payment plus the principal repayment.
The cash flow (CF) in the final year of a bond's life consists of two components: the last periodic interest payment and the repayment of the principal (face value). For Company A's bond, this

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May/June 2017

100. A bond that grants the issuer the right to repay the bond before maturity is a _____, while a bond that grants the holder the right to demand early repayment is a _____.
(A) callable bond; putable bond
(B) putable bond; callable bond
(C) convertible bond; subordinated bond
(D) zero-coupon bond; fixed-rate bond

Ans :

(A) callable bond; putable bond
A callable bond contains a call option, which gives the issuer the right to redeem the bond prior to its scheduled maturity. A putable bond contains a put option, which gives the bondholder the right to sell the bond back to the issuer before maturity. These options benefit the issuer and holder, respectively.

Oct/Nov 2005

101. Which of the following correctly pairs a bond type with its primary characteristic?
(A) Inflation-indexed bond: Its coupon payment is linked to a broad economic indicator like GDP growth.
(B) Asset-backed security: The pool of assets backing the security remains on the issuer's balance sheet.
(C) Perpetual bond: The principal is repaid only after an extremely long period, such as 100 years.
(D) Convertible bond: Can be exchanged for a set number of the issuer's common stock shares.

Ans :

(D) Convertible bond: Can be exchanged for a set number of the issuer's common stock shares.
A convertible bond's defining feature is the option it gives the holder to convert the debt instrument into a specified number of equity shares. The other pairs are incorrect: inflation-indexed bonds are linked to an inflation index, ABS assets are typically off-balance sheet, and perpetual bonds have no principal repayment date.

May/June 2020

102. Identify the incorrect statement regarding the tax treatment of corporate financing.
(A) Interest payments on debt are tax-deductible.
(B) Interest payments on debt and dividend payments on equity receive identical tax treatment.
(C) Dividend payments on equity are not tax-deductible.
(D) Debt capital provides a 'tax-shield' for the issuing firm.

Ans :

(B) Interest payments on debt and dividend payments on equity receive identical tax treatment.
There is a differential tax treatment for debt and equity. Interest payments on debt are treated as an expense and are tax-deductible, reducing the firm's taxable income. In contrast, dividend payments to shareholders are paid out of after-tax profits and are not tax-deductible for the firm. This makes their tax treatment fundamentally different.

Oct/Nov 2015

103. Match List-I (Bond Term) with List-II (Description).
List-I
P. Coupon Rate
Q. YTM
R. Face Value
S. Duration
List-II
1. The principal amount to be repaid at maturity.
2. The holding period where interest rate risk is neutralized.
3. The fixed rate of interest paid on the bond.
4. The total return if the bond is held to maturity.
(A) P-3, Q-4, R-1, S-2
(B) P-4, Q-3, R-2, S-1
(C) P-3, Q-1, R-4, S-2
(D) P-1, Q-2, R-3, S-4

Ans :

(A) P-3, Q-4, R-1, S-2
The correct matching is as follows: P (Coupon Rate) is the fixed rate of interest (3). Q (YTM) is the total return if held to maturity (4). R (Face Value) is the principal amount repaid at maturity (1). S (Duration) is the holding period that neutralizes interest rate risk (2).

May/June 2013

104. Consider the following statements about bond valuation:
1. If the required rate of return is less than the coupon rate, the bond's value is greater than

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The magnitude of the price increase (2.94%) resulting from a 1% rate fall is different from the magnitude of the price decrease (2.83%) resulting from a 1% rate rise. This demonstrates the asymmetrical nature of bond price volatility, a concept also known as convexity, where the upside price movement is larger than the downside movement.

Oct/Nov 2006

85. A bond has a face value of ₹500, a market price of ₹420, a 12% coupon, and 4 years to maturity. The holder's income tax rate is 30% and capital gains tax is 15%. What is the post-tax annual income from the coupon payment?
(A) ₹42
(B) ₹60
(C) ₹18
(D) ₹51

Ans :

(A) ₹42
The annual coupon payment is 12% of the ₹500 face value, which is ₹60. Since this income is taxed at a rate of 30%, the post-tax income is calculated as the pre-tax income multiplied by $(1 - \text{tax rate})$. Therefore, the post-tax income is ₹60 × (1 - 0.30) = ₹60 × 0.70 = ₹42.

May/June 2021

86. For the bond in the previous question (Face Value ₹500, Market Price ₹420), what is the redemption value after adjusting for the 15% capital gains tax?
(A) ₹500
(B) ₹488
(C) ₹420
(D) ₹428

Ans :

(B) ₹488
The capital gain is the difference between the redemption value (face value of ₹500) and the purchase price (market price of ₹420), which is ₹80. The capital gains tax is 15% of this gain: $0.15 \times 80 = 12$. The redemption value after tax is the face value minus the tax: ₹500 - ₹12 = ₹488.

Oct/Nov 2010

87. An approximate formula for post-tax YTM is given as

$$\frac{I(1-t)+(F-P)/n}{0.4F+0.6P}.$$

What does the term (F-P)/n in the numerator represent?
(A) The annual coupon interest.
(B) The total capital gain on the bond.
(C) The average price of the bond.
(D) The annualized capital gain or loss.

Ans :

(D) The annualized capital gain or loss.
In this approximation formula, 'F' is the redemption value and 'P' is the purchase price. The difference (F-P) is the total capital gain or loss over the bond's life. Dividing this by 'n', the number of years to maturity, effectively spreads the gain or loss evenly over the holding period, representing an annualized figure.

May/June 2005

88. After calculating a bond's post-tax YTM and its duration of 3.51 years, what is the next logical step to quantify its interest rate risk?
(A) Calculate the interest rate elasticity.
(B) Calculate the bond's current yield.
(C) Recalculate the bond's market price.
(D) Find the pre-tax YTM.

Ans :

(A) Calculate the interest rate elasticity.
After determining the duration (D) and the YTM, the next logical step to quantify interest rate risk is to compute the interest rate elasticity (IE).
This is done using a formula such as

$$\text{IE} = \frac{-\text{D} \times \text{YTM}}{1 + \text{YTM}}$$

Elasticity provides a direct measure of the percentage price change for a given percentage change in yield.

Oct/Nov 2022

89. The interest rate elasticity for a bond is calculated as -0.409. What will be the sign of the percentage price change if interest rates fall?
(A) Negative, as the bond price will fall.
(B) Zero, as the price will not change.
(C) Positive, as the bond price will rise.
(D) It cannot be determined from the elasticity.

Ans :

(C) Positive, as the bond price will rise.
A fall in interest rates leads to a rise in bond prices due to their inverse relationship. The formula for percentage price change involves multiplying the negative elasticity (-0.409) by the percentage change in YTM. A fall in rates means the change

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payments received by the investor are reinvested at the interest rate prevailing in the market at the time they are received. This reinvestment return is a key component of the bond's total return.

Oct/Nov 2015

61. The concept of a bond's duration arises from the trade-off between which two factors when market interest rates change?
(A) Credit risk and liquidity risk.
(B) Coupon rate and maturity date.
(C) Face value and redemption value.
(D) Market price of the bond and reinvestment of coupon receipts.

Ans :

(D) Market price of the bond and reinvestment of coupon receipts.
When market interest rates rise, the market price of a bond falls (price risk), but the investor gains by reinvesting coupon payments at a higher rate (reinvestment gain). Duration is the point in time (holding period) at which the loss from the price decrease is exactly offset by the gain from reinvesting coupons.

May/June 2013

62. What is Macaulay Duration?
(A) A portfolio-level metric calculated as the weighted average of individual bond durations.
(B) The holding period that immunizes an investor from interest rate risk.
(C) The specific time remaining until a bond's market price converges with its par value.
(D) A direct measure of a bond's price volatility, named after its creator, Frederick Macaulay.

Ans :

(B) The holding period that immunizes an investor from interest rate risk.
Macaulay Duration represents the specific holding period at which an investor is immunized from interest rate risk. It is the point where the negative impact of a price change (price risk) is perfectly offset by the positive impact on the reinvestment of coupons (reinvestment risk), ensuring the investor achieves the anticipated yield.

Oct/Nov 2021

63. What is the first step in computing the Macaulay Duration of a bond?
(A) Determine the present value of the cash flows.
(B) Multiply present values by the time until receipt.
(C) Determine the cash flows from holding the bond.
(D) Divide the sum of products by the total present value.

Ans :

(C) Determine the cash flows from holding the bond.
The process of calculating Macaulay Duration begins with identifying all the future cash flows the bond will generate. This involves listing each periodic coupon payment and the final principal repayment at maturity. These cash flows are the foundation for all subsequent steps in the duration calculation, which involves weighting them by time.

May/June 2024

64. The formula for Macaulay Duration is given by

$$\text{Duration} = \frac{\sum(pv \times T)}{\sum pv}$$

What does the numerator, $\sum(pv \times T)$, represent?
(A) The sum of all future cash flows (coupons and principal) without any discounting.
(B) The simple arithmetic mean of the time periods (1, 2, ... n) until cash flows are received.
(C) The total present value of all cash flows, which is also known as the bond's market price.
(D) The sum of the time-weighted present values of each cash flow.

Ans :

(D) The sum of the time-weighted present values of each cash flow.
The numerator of the Macaulay Duration formula, $\sum(pv \times T)$, represents the sum of time-weighted present values of cash flows. Each cash flow's present value (pv) is multiplied by the time period (T) in which it is received, and these products are then summed up. This gives more weight to later cash flows.

Oct/Nov 2008

65. A 5-year bond with a 12.5% coupon is redeemable at a 5% premium on its ₹100 face value. The expected market rate is 15%. If its duration is

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(callable), a put option (putable), both a put and a call option, or no options at all (a straight bond). Callability and putability are features that can be included in a bond's structure.

Oct/Nov 2019

95. Which of the following is a correct statement about zero-coupon bonds?
(A) The holder receives the full principal amount at redemption.
(B) They pay regular, fixed interest payments on a semi-annual basis.
(C) They are initially issued at a price higher than their stated par value.
(D) They are a type of debt instrument issued exclusively by government entities.

Ans :

(A) The holder receives the full principal amount at redemption.
A key feature of a zero-coupon bond is that while it is bought at a discount, the bondholder is entitled to receive the full principal (par) amount upon the bond's maturity or redemption date. The other statements are incorrect: they pay no regular interest and are issued at a discount, not a premium.

May/June 2009

96. Using a standard present value table, what is the Present Value Interest Factor (PVIF) for a single sum to be received in 8 years if the interest rate is 9% per year?
(A) 0.540
(B) 0.502
(C) 0.460
(D) 0.424

Ans :

(B) 0.502
To find the PVIF, you locate the row corresponding to the "Number of Years" (8) and the column corresponding to the "Interest Rate per Year" (9%). The value at the intersection of the 8-year row and the 9% column in a standard PVIF table is 0.502. This means ₹1 received in 8 years is worth ₹0.502 today at a 9% discount rate.

Oct/Nov 2011

97. According to a standard present value table, what is the present value of ₹1 to be received 5 years from now, if the interest rate is 10% per year?
(A) 0.683
(B) 0.621
(C) 0.567
(D) 0.784

Ans :

(B) 0.621
By referencing a Present Value Interest Factor (PVIF) table, one must find the intersection of the row for 5 years and the column for a 10% interest rate. The value provided in the table at this specific coordinate is 0.621. This factor represents the present value of a single rupee to be received in five years' time.

May/June 2010

98. Using a standard present value of annuity table, what is the Present Value Interest Factor of an Annuity (PVIFA) for a period of 10 years at an interest rate of 8% per year?
(A) 6.710
(B) 7.360
(C) 7.722
(D) 6.247

Ans :

(A) 6.710
To determine the PVIFA from a standard table, you need to find the value at the intersection of the row for the "Number of Years" (10) and the column for the "Interest Rate per Year" (8%). The table shows this value to be 6.710. This factor is used to calculate the present value of ten equal annual payments.

Oct/Nov 2024

99. A note in a financial table states that if the interest rate is 10% per year, the value of ₹1 received in each of the next 5 years is ₹3.791. What does this value represent?
(A) The PVIF for 5 years at 10%.
(B) The total sum of payments (₹5).
(C) The PVIFA for 5 years at 10%.
(D) The future value of ₹1 for 5 years.

Ans :

(C) The PVIFA for 5 years at 10%.
The value ₹3.791 represents the present value of an annuity of ₹1 per period for 5 periods at a 10% interest rate. This is, by definition, the Present Value Interest Factor of an Annuity (PVIFA). This can be confirmed by looking at the intersection of the 5-year row and 10% column in a PVIFA table.

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(A) $\frac{1+r}{r}$

(B) $\frac{1}{r}$

(C) $\frac{1}{1+r}$

(D) $\frac{r}{1+r}$

Ans :

(A) $\frac{1+r}{r}$

A specific property of duration states that for a perpetual bond, which has no maturity date, the duration can be calculated using a simple formula. The duration is equal to $\frac{1+r}{r}$, where 'r' represents the current yield of the bond. This provides a finite measure for an infinite stream of payments.

Oct/Nov 2012

71. How are Duration and YTM related, according to the properties of duration?
(A) They are directly related.
(B) They are unrelated.
(C) They are equal for all bonds.
(D) They are inversely related.

Ans :

(D) They are inversely related.
One of the key properties of duration is that it is inversely related to the Yield-to-Maturity (YTM). This means that as a bond's YTM increases, its duration decreases. A higher discount rate (YTM) reduces the present value of distant cash flows more heavily, thus shortening the weighted-average time to receipt of cash flows.

May/June 2011

72. How does an increase in the frequency of coupon payments (e.g., from annual to semi-annual) affect a bond's duration?
(A) It increases the duration.
(B) It decreases the duration.
(C) It has no effect on the duration.
(D) The effect depends on the coupon rate.

Ans :

(B) It decreases the duration.
An increase in the frequency of coupon payments leads to a decrease in the bond's duration. This is because cash flows are received sooner, which reduces the weighted-average time to receipt of the bond's total cash flows. A decrease in payment frequency would have the opposite effect, increasing the duration.

Oct/Nov 2020

73. What is the term for the sensitivity of a bond's price to changes in interest rates?
(A) Credit Spread
(B) Reinvestment Risk
(C) Bond Price Volatility
(D) Default Premium

Ans :

(C) Bond Price Volatility
Bond Price Volatility is the term used to describe the sensitivity of a bond's price to changes in market interest rates or yields. It measures the extent of the price change for a given change in YTM and is a key indicator of the bond's interest rate risk. Duration is a primary tool for measuring this volatility.

May/June 2022

74. Interest Rate Elasticity (IE) of a bond is always a negative number. Why?
(A) Because interest rates can never be negative.
(B) Because coupon payments are always positive.
(C) Because bond duration is always less than maturity.
(D) Because bond prices and YTM are inversely related.

Ans :

(D) Because bond prices and YTM are inversely related.
Interest Rate Elasticity (IE) measures the percentage change in price for a percentage change in yield. Due to the fundamental inverse relationship between bond prices and YTM, an increase in yield leads to a price decrease, and vice versa. This opposite movement ensures that the resulting elasticity calculation will always be a negative number.

Oct/Nov 2023

75. Interest Rate Elasticity (IE) can be calculated using the formula

$$\text{IE} = -\text{Modified Duration} \times \text{YTM}$$

What does this relationship imply?
(A) Duration and interest rate elasticity are directly related.
(B) Duration and interest rate elasticity are inversely related.

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its par value.
2. If the required rate of return is greater than the coupon rate, the bond's value is less than its par value.

Which of the statements is/are correct?
(A) Only 1
(B) Only 2
(C) Both 1 and 2
(D) Neither 1 nor 2

Ans :

(C) Both 1 and 2
Both statements are correct and represent fundamental theorems of bond valuation. A bond paying a coupon higher than the prevailing market rate is more desirable, so its price is bid up above par (a premium). A bond paying a coupon lower than the market rate is less desirable, so its price falls below par (a discount).

Oct/Nov 2021

105. **Assertion (A) :** A bond with a longer term to maturity will experience a greater price change for a given change in YTM compared to a shorter-term bond.
Reason (R) : In the case of long-maturity bonds, a change in YTM is cumulatively applied to a longer series of coupon payments and a more distant principal repayment.
(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
Assertion (A) is a correct statement of bond price sensitivity. Reason (R) correctly explains why this occurs. The discounting effect of a YTM change is magnified over a greater number of periods, impacting a longer stream of cash flows. This makes the present value of a longer-term bond more sensitive to discount rate changes.

May/June 2024

106. Which of the following statements is incorrect regarding the properties of duration?
(A) The duration of a zero-coupon bond is equal to its term to maturity.
(B) A larger coupon rate leads to a larger duration.
(C) Duration and YTM are inversely related.
(D) Duration is generally less than the term to maturity for a coupon-paying bond.

Ans :

(B) A larger coupon rate leads to a larger duration. This statement is incorrect. A larger coupon rate leads to a smaller duration. This is because higher coupon payments mean the investor receives a larger portion of the bond's total cash flow sooner, which reduces the weighted-average time to receipt of cash flows (duration). The other statements are correct properties of duration.

Oct/Nov 2008

107. Consider the following statements:
1. Macaulay Duration is calculated as Modified Duration / (1 + YTM).
2. Interest Rate Elasticity is always a positive number.
3. Bond price volatility measures the sensitivity of bond price to interest rate changes.

Which of the statements is/are correct?
(A) Only 3
(B) 1 and 2
(C) 2 and 3
(D) 1, 2 and 3

Ans :

(A) Only 3
Statement 3 is correct. Statement 1 is incorrect; the formula is reversed

$$\text{Modified Duration} = \frac{\text{Macaulay Duration}}{1 + \text{YTM}}$$

Statement 2 is incorrect; Interest Rate Elasticity is always negative due to the inverse relationship between price and yield. Therefore, only the third statement accurately describes a concept from the chapter.

May/June 2006

108. An investor purchases a 10-year, 8% coupon bond with a par value of ₹1,000 at a price of ₹950. Immediately after purchase, market interest rates rise to 9%. Which of the following will occur?
(A) The bond's market price will decrease, while reinvestment income will increase.
(B) The bond's market price will increase, while reinvestment income will decrease.
(C) The bond's market price will increase, and reinvestment income will also increase.
(D) The bond's market price will decrease, and

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Ans :

(D) Exactly 3.99 years
Duration is the holding period that balances price risk and reinvestment risk. If an investor's holding period or investment horizon is equal to the bond's duration, the realized return will be locked in and unaffected by subsequent changes in market interest rates. A mismatch between horizon and duration creates interest rate risk.

May/June 2021

128. If a bond's YTM is lower than its coupon rate, it will trade at a premium. As this bond approaches maturity, its price will:
(A) Decrease towards its par value
(B) Increase further
(C) Remain constant at the premium price
(D) Fluctuate unpredictably

Ans :

(A) Decrease towards its par value
This is a direct application of a bond valuation theorem. A bond trading at a premium (price > par) will see its price gradually fall over its remaining life, ultimately converging to its par value at the maturity date. This process is known as the "pull to par" effect, which applies to both premium and discount bonds.

Oct/Nov 2010

129. What is the fundamental reason that debt capital provides a 'tax-shield' to a company?
(A) Governments have a stated policy goal to encourage corporate borrowing.
(B) Bondholders pay tax on their income, so the company is exempt.
(C) Interest payments are considered a tax-deductible business expense.
(D) Dividend payments made to shareholders are given a special tax credit.

Ans :

(C) Interest payments are considered a tax-deductible business expense.
The tax-shield from debt arises because tax laws in most jurisdictions allow companies to deduct interest payments from their income before calculating taxes. This lowers the company's taxable income and, consequently, its tax liability. Dividends, paid from after-tax profits, do not offer this benefit.

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May/June 2005

130. An investor buys a bond at ₹900. It has a face value of ₹1,000 and matures in 5 years. If held to maturity, the investor will realize a:
(A) Capital gain of ₹100
(B) Capital loss of ₹100
(C) Capital gain of ₹500
(D) No capital gain or loss

Ans :

(A) Capital gain of ₹100
A capital gain or loss on a bond held to maturity is the difference between its redemption value (typically the face value) and its purchase price. In this case, the investor bought the bond for ₹900 and will receive ₹1,000 at maturity. This results in a capital gain of ₹1,000 - ₹900 = ₹100.

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(A) To finance short-term working capital needs.
(B) To speculate on interest rate movements.
(C) To finance long-term investments.
(D) To reduce the company's equity base.

Ans :

(C) To finance long-term investments.
The text explicitly states that bonds provide the borrower with external funds to finance long-term investments. As long-term instruments themselves, they are a suitable source of capital for projects and assets that have a long useful life, matching the maturity of the funding with the maturity of the investment.

May/June 2011

114. Consider the following statements regarding bond features:
1. Covered bonds are backed by assets that remain on the issuer's balance sheet.
2. Asset-backed securities are backed by assets that are moved to a separate entity.
3. Subordinated bonds have a higher repayment priority than senior bonds.

Which combination of statements is correct?
(A) 1 and 2 only
(B) 1 and 3 only
(C) 2 and 3 only
(D) 1, 2, and 3

Ans :

(A) 1 and 2 only
Statements 1 and 2 correctly describe the key difference between covered bonds and asset-backed securities. Statement 3 is incorrect; subordinated bonds have a lower priority (are junior) to senior bonds in the event of liquidation, meaning they get paid only after senior bondholders are fully compensated.

Oct/Nov 2020

115. A bond's value is calculated as ₹1,049.44 when the discount rate is 10%. If the discount rate were to increase to 11%, what would happen to the bond's value?
(A) It would decrease to below ₹1,049.44.
(B) It would increase to above ₹1,049.44.
(C) It would remain at ₹1,049.44.
(D) It would become equal to the par value.

Ans :

(A) It would decrease to below ₹1,049.44.
Due to the inverse relationship between bond prices and interest rates (yields), an increase in the discount rate from 10% to 11% will cause the present value of the bond's future cash flows to decrease. Therefore, the bond's calculated value will fall below its previous value of ₹1,049.44.

May/June 2022

116. If a bond with annual interest payments has a value of ₹1,049.44, an otherwise identical bond that pays semi-annual interest would have a value that is:
(A) Lower than ₹1,049.44
(B) Higher than ₹1,049.44
(C) Exactly ₹1,049.44
(D) Impossible to determine without more information.

Ans :

(B) Higher than ₹1,049.44
A bond with semi-annual interest payments is more valuable because the investor receives cash flows sooner, allowing for earlier reinvestment. The text explicitly states that "the value of such bonds would be more than the value of bonds with an annual interest payment" due to the reinvestment of the half-yearly interest.

Oct/Nov 2023

117. An investor buys a bond with a 5-year maturity and a YTM of 10%, intending to hold it to maturity. Immediately after purchase, market interest rates fall to 9%. What is the impact on the investor's position if they hold the bond for less than its duration?
(A) Their total yield will be exactly 10%.
(B) Their total yield will be more than 10%.
(C) Their total yield will be less than 10%.
(D) Their total yield will be 9%.

Ans :

(B) Their total yield will be more than 10%.
When rates fall, the bond's price increases. If the investor sells before reaching the duration point, the capital gain from the price increase will more than offset the loss from reinvesting coupons at the new, lower rate. Therefore, their realized yield for that shorter holding period will be greater than the originally anticipated 10%.

May/June 2016

118. Which of the following statements is correct?
1. For a premium bond, the price declines

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reinvestment income will also decrease.

Ans :

(A) The bond's market price will decrease, while reinvestment income will increase.
When market interest rates rise, the price of existing, lower-coupon bonds falls, creating a price risk. However, the investor benefits from being able to reinvest the periodic coupon payments at the new, higher market rate, resulting in a reinvestment gain. The concept of duration balances these two opposing effects.

Oct/Nov 2017

109. Identify the incorrect pair of a day count convention and its description.
(A) Actual/Actual: Actual number of days are calculated.
(B) Actual/360: Interest for a year is calculated assuming 360 days in a year.
(C) Actual/365: Days in a leap year are considered as 366.
(D) 30/360: The days of the month are assumed at 30 for interest calculation.

Ans :

(C) Actual/365: Days in a leap year are considered as 366.
The description for the Actual/365 convention states that even in the case of a leap year, the days in the year would be considered as 365. This means the denominator is always 365, regardless of whether the actual year has 365 or 366 days. The other pairs are correctly described.

May/June 2008

110. A bond is described as being 'highly liquid in the secondary market'. What does this imply?
(A) It can be easily bought or sold, allowing ownership transfer.
(B) The bond offers a very high coupon rate relative to the market.
(C) The bond is very close to its final maturity and redemption date.
(D) The bond is issued by a sovereign government entity with high credit quality.

Ans :

(A) It can be easily bought or sold, allowing ownership transfer.
Liquidity refers to the ease with which an asset can be bought or sold in the market without affecting its price. A highly liquid bond means that its ownership can be readily transferred through trading in the secondary market, allowing investors to enter or exit their positions without difficulty.

Oct/Nov 2013

111. Which of the following is NOT a characteristic of debentures issued by private sector companies in India, as described in the text?
(A) They are a form of debt capital.
(B) They make the holder a creditor of the firm.
(C) Interest paid on them is tax-deductible for the issuer.
(D) They are entirely free from the risk of default.

Ans :

(D) They are entirely free from the risk of default.
The text states that bonds of public sector companies are generally secured but not free from default risk, and implies the same for private sector debentures. Only bonds issued by the government are described as having no risk of default. Corporate debentures always carry some level of credit or default risk.

May/June 2015

112. A company issues a 10-year bond with a face value of ₹100 and a 10% coupon rate. Irrespective of the company's profits or losses, the bondholder is entitled to receive:
(A) A variable share of the company's annual profits, paid as a dividend.
(B) An annual payment of ₹10 for 10 years, plus ₹100 at maturity.
(C) A single lump-sum payment of ₹110 at the end of the 10th year only.
(D) An annual payment amount that fluctuates with the company's stock price.

Ans :

(B) An annual payment of ₹10 for 10 years, plus ₹100 at maturity.
The bond contract guarantees specific payments. A 10% coupon on a ₹100 face value means the holder receives ₹10 in interest each year. The contract also obligates the issuer to repay the face value of ₹100 at maturity. These payments are legally binding, regardless of the company's financial performance.

Oct/Nov 2012

113. What is the primary purpose for which bonds are issued by borrowers like firms and governments?

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4. Risky because it can be lost or stolen.

(A) P-2, Q-3, R-1, S-4
(B) P-4, Q-1, R-2, S-3
(C) P-4, Q-2, R-1, S-3
(D) P-1, Q-4, R-3, S-2

Ans :

(B) P-4, Q-1, R-2, S-3
The correct matching is as follows: P (Bearer Bond) is risky because it can be lost or stolen (4). Q (Subordinated Bond) has a lower priority in liquidation (1). R (High-Yield Bond) is rated below investment grade (2). S (Government Bond) is considered free from default risk (3).

Oct/Nov 2025

123. A bond's coupon rate is 10%. If the required rate of return (k_d) is also 10%, what is the relationship between the bond's value (V_0), its par value, its current yield, and its YTM?

(A) V_0 > Par; Current Yield < YTM
(B) V_0 < Par; Current Yield > YTM
(C) V_0 = Par; Current Yield = YTM
(D) V_0 = Par; Current Yield < YTM

Ans :

(C) V_0 = Par; Current Yield = YTM
When the required rate of return equals the coupon rate, the bond's value is equal to its par value. In this case, since the price is par, the current yield (Coupon/Price) will also be equal to the coupon rate (10%). By definition, the YTM is also 10%. Thus, all measures are equal.

May/June 2012

124. Consider these four types of bonds:

1. Fixed rate bond
2. Floating rate note
3. Zero-coupon bond
4. Convertible bond

Which of these are categorized based on their interest payment structure?

(A) 1, 2, and 4
(B) 1 and 3 only
(C) 1, 2, and 3
(D) All of the above

Ans :

(C) 1, 2, and 3
Fixed rate, floating rate, and zero-coupon bonds are all defined by how they pay interest. A fixed rate bond has a constant coupon, a floating rate note has a variable coupon, and a zero-coupon bond pays no regular interest. A convertible bond is defined by its conversion feature, not its interest payment structure.

Oct/Nov 2014

125. Which of the following statements about the relationship between Macaulay Duration (MD), Modified Duration (ModD), and Yield-to-Maturity (YTM) is correct?

(A) $\text{ModD} = \frac{\text{MD}}{1 + \text{YTM}}$
(B) $\text{IE} = -\text{MD} \times \text{YTM}$
(C) $\text{IE} = -\text{ModD} \times (1 + \text{YTM})$
(D) $\text{MD} = \text{ModD} \times \text{YTM}$

Ans :

(A) $\text{ModD} = \frac{\text{MD}}{1 + \text{YTM}}$
The correct relationship is that Modified Duration is derived from Macaulay Duration by dividing by (1 + YTM). The other options misstate the standard formulas. For instance, Interest Rate Elasticity (IE) is related to Modified Duration, not Macaulay Duration directly in simple formulas. Therefore, the chosen option is the correctly stated formula.

May/June 2019

126. A bond's price is more sensitive to a 1% drop in yield than to a 1% rise in yield. This property is an illustration of the bond's:

(A) Negative convexity
(B) Positive convexity
(C) Negative duration
(D) Credit risk

Ans :

(B) Positive convexity
The phenomenon where a bond's price increases more for a given drop in yield than it decreases for the same rise in yield is known as positive convexity. This asymmetrical response is a favorable characteristic for bondholders, as it implies greater upside potential than downside risk for parallel yield shifts.

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Oct/Nov 2006

127. If a bond has a duration of 3.99 years, this implies that the investor is immunized from interest rate risk if their investment horizon is:

(A) 5 years, the bond's maturity
(B) Less than 3.99 years
(C) Greater than 3.99 years
(D) Exactly 3.99 years

a country's currency is normally had only within that country.

Ans :

(D) The principle that the useful possession of a country's currency is normally had only within that country.
A fundamental aspect of foreign exchange is that almost every country has its own unique currency (legal tender), and its practical use is generally confined within that country's borders. This necessitates a mechanism to exchange currencies when dealing with international transactions, as one currency is not typically useful in another country.

Oct/Nov 2008

5. How are exchanges from one currency to another mostly put through by banks?
(A) Through the physical transportation of currency notes between countries via secured air freight.
(B) By issuing a globally accepted promissory note that is backed by the World Bank.
(C) By means of bookkeeping entries carried out in the two concerned financial centres.
(D) Through the direct barter of goods and services to avoid the use of any currency.

Ans :

(C) By means of bookkeeping entries carried out in the two concerned financial centres.
The mechanism of foreign exchange largely relies on banks executing bookkeeping entries in the two relevant financial centers. This method avoids the cumbersome and risky physical transfer of large amounts of cash. Instead, correspondent bank accounts are debited and credited to effect the transfer of value from one currency to another efficiently.

May/June 2022

6. What instruments are predominantly used to effect the exchange of one currency for another?
(A) Precious metals such as gold and silver, which serve as a universal store of value.
(B) Credit instruments, which represent a claim to payment between parties.
(C) Physical commodities like oil or grain, which can be traded internationally.
(D) Corporate stocks and bonds issued by multinational corporations.

Ans :

(B) Credit instruments, which represent a claim to payment between parties.
Almost all exchanges of one currency for another are facilitated with the help of credit instruments. These instruments, such as bills of exchange, letters of credit, and electronic fund transfers, represent a claim to payment and are the primary tools used by the banking system to manage and execute cross-border currency transactions and settlements.

Oct/Nov 2011

7. What is the primary reason that exchange rate movements in the Indian forex market do not always follow the international trend in the short run?
(A) The widespread and exclusive use of the barter system for foreign trade in India.
(B) The Indian market's complete technical and regulatory isolation from all global financial systems.
(C) The fixed valuation of the Indian Rupee against a specific basket of commodities like oil and gold.
(D) The restriction on the free flow of capital, which limits funds moving into or out of the country.

Ans :

(D) The restriction on the free flow of capital, which limits funds moving into or out of the country.
The Indian forex market's exchange rate movements can diverge from international trends, particularly in the short run, mainly due to restrictions on the free flow of capital. These capital controls limit the extent to which foreign investment can enter or exit the country, thereby insulating the domestic market from some global pressures.

May/June 2014

8. Prior to the implementation of the 'Liberalised Exchange Rate Management System' (LERMS), how were exchange rates managed in India?
(A) The Reserve Bank of India (RBI) administratively fixed the buying and selling rates.
(B) Rates were freely determined by global market forces without any central bank intervention.

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CHAPTER 23

Financial Mathematics – Forex Arithmetic

Oct/Nov 2015

1. What is the primary function of 'Foreign Exchange' in the context of banking?

(A) To facilitate domestic trade transactions between different states within a country.

(B) To provide a mechanism for converting the currency of one country into that of another.

(C) To exclusively set the official interest rates for all types of international loans.

(D) To regulate the flow of investment capital within the borders of a single country.

Ans :

(B) To provide a mechanism for converting the currency of one country into that of another.

Foreign Exchange refers to the general mechanism by which a bank converts one country's currency into another's. This process is essential for settling international trade, where payments need to be made and received in different national currencies, thereby facilitating the transfer of funds across borders for goods, services, and finance.

May/June 2007

2. Foreign trade transactions are typically expressed and paid for in which of the following currencies?

(A) In the currency of the exporter, the importer, or a mutually acceptable third country.

(B) Only in the currency of the exporter's country to prevent any exchange rate risk for the seller.

(C) Only in the currency of the importer's country to simplify the process of payment settlement.

(D) Only in a neutral, internationally agreed-upon currency like Special Drawing Rights (SDRs).

Ans :

(A) In the currency of the exporter, the importer, or a mutually acceptable third country.

Foreign trade can be transacted in the currency of the exporter's country, the importer's country, or a third country's currency like the US Dollar or Pound Sterling, provided it is acceptable to both parties. This flexibility necessitates a robust foreign exchange mechanism to handle the required currency conversions for final settlement.

Oct/Nov 2024

3. What does the term 'concomitant of foreign trade' imply about foreign exchange?

(A) It is an optional tool in foreign trade, typically reserved only for very large transactions.

(B) It is primarily a barrier to foreign trade that significantly increases overall transaction costs.

(C) It is a natural and inseparable accompaniment to the process of conducting foreign trade.

(D) It is an independent economic system that primarily serves functions other than foreign trade.

Ans :

(C) It is a natural and inseparable accompaniment to the process of conducting foreign trade.

The statement that foreign exchange is a concomitant of foreign trade means it naturally accompanies or is associated with it. International trade inherently involves different currencies, making the conversion of one currency to another an essential and unavoidable part of settling transactions between importers and exporters from different countries.

May/June 2019

4. Which of the following is identified as a fundamental aspect of the foreign exchange mechanism?

(A) The requirement that all countries share a single, universal currency for all international trade.

(B) The process where currency exchanges are primarily conducted using physical cash transfers.

(C) The system where individuals, not banks, are the primary facilitators of currency exchange.

(D) The principle that the useful possession of

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towards par as maturity approaches.
2. For a discount bond, the price declines towards par as maturity approaches.
3. For a par bond, the price remains at par as maturity approaches, assuming the discount rate equals the coupon rate.

(A) 1 and 3 only
(B) 1 and 2 only
(C) 2 and 3 only
(D) 1, 2, and 3

Ans :

(A) 1 and 3 only
Statement 1 is correct (a premium bond's price falls towards par). Statement 3 is also correct (a par bond's price stays at par if rates are stable). Statement 2 is incorrect; for a discount bond, the price increases towards par value as maturity approaches, it does not decline. Therefore, only statements 1 and 3 are correct.

Oct/Nov 2009

119. A bond is considered risky for an investor if:
(A) The bond's fixed coupon rate is different from its current yield to maturity.
(B) The bond is trading at a premium price, i.e., above its par value.
(C) The investor's holding period is different from the bond's duration.
(D) The bond is issued by a private corporation rather than a government body.

Ans :

(C) The investor's holding period is different from the bond's duration.
The text defines interest rate risk in the context of duration. It states that "a bond will be risky if the holding period of the bond is different from its duration." This is because a mismatch between the holding period and duration exposes the investor to a net gain or loss from interest rate changes.

May/June 2023

120. **Assertion (A) :** The duration of a coupon-paying bond is always less than its term to maturity.
Reason (R) : Some of the bond's cash flows (the coupons) are received before the final maturity date, which pulls the weighted-average time of cash flows to a point earlier than maturity.
(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true, but (R) is not the correct explanation of (A).
(C) (A) is true, but (R) is false.
(D) (A) is false, but (R) is true.

Ans :

(A) Both (A) and (R) are true, and (R) is the correct explanation of (A).
Assertion (A) is a fundamental property of duration for coupon bonds. Reason (R) provides the precise logic for this property. Since duration is the weighted-average timing of all cash flows, the receipt of coupon payments before the final principal repayment necessarily makes this average time shorter than the final maturity date.

Oct/Nov 2018

121. An investor holds two bonds with the same maturity and YTM. Bond A has an 8% coupon, and Bond B has a 4% coupon. Which bond will have a higher duration and greater price volatility?
(A) Bond A will have a higher duration and greater price volatility.
(B) Both bonds will have the same duration and price volatility.
(C) It is impossible to determine without knowing the maturity.
(D) Bond B will have a higher duration and greater price volatility.

Ans :

(D) Bond B will have a higher duration and greater price volatility.
According to the properties of duration, a lower coupon rate results in a longer duration. This is because a larger proportion of the bond's total return comes from the final principal payment. A longer duration, in turn, implies greater price sensitivity or volatility to changes in interest rates. Therefore, Bond B is more volatile.

May/June 2007

122. Match List-I (Bond Type) with List-II (Risk/ Feature).
List-I
P. Bearer Bond
Q. Subordinated Bond
R. High-Yield Bond
S. Government Bond
List-II
1. Lower priority in case of liquidation.
2. Rated below investment grade.
3. Not exposed to default risk.

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(C) Rates were determined solely by the supply and demand within the local interbank market.
(D) Rates were pegged to the international price of gold, with adjustments made on a daily basis.

Ans :

(A) The Reserve Bank of India (RBI) administratively fixed the buying and selling rates.
Before the introduction of LERMS, the forex market in India was tightly controlled. The Reserve Bank of India played a direct role by fixing both the buying and selling rates for foreign currencies. The market was required to operate within the ceiling and floor rates established by the central bank, limiting rate volatility.

Oct/Nov 2006

9. At present, what are the primary drivers of the exchange rate in the Indian forex market?
(A) The daily directives on mandatory exchange rates issued by the Reserve Bank of India.
(B) The international price of crude oil, which exclusively determines the rate on a daily basis.
(C) The forces of demand and supply interacting within the local interbank market.
(D) A fixed peg to the US Dollar that is strictly maintained by the Indian government.

Ans :

(C) The forces of demand and supply interacting within the local interbank market.
Currently, following the implementation of the Liberalised Exchange Rate Management System (LERMS), the exchange rate in India is primarily driven by the market forces of demand and supply. The interaction between buyers and sellers in the local interbank market determines the value of the Indian Rupee against other currencies on a daily basis.

May/June 2025

10. How is a currency quotation defined in the context of foreign exchange?
(A) The price of one currency expressed in terms of another currency.
(B) The specific interest rate charged on a foreign currency loan or deposit.
(C) The total volume of a particular currency traded globally in a single day.
(D) The official government forecast for a currency's expected future value.

Ans :

(A) The price of one currency expressed in terms of another currency.
A currency quotation, or exchange rate, is simply the price of one country's currency expressed in terms of another country's currency. For instance, a quotation of $1 = ₹75.00 indicates that one US dollar can be exchanged for seventy-five Indian rupees, establishing a price for the dollar relative to the rupee.

Oct/Nov 2019

11. For an Indian national, which of the following represents a direct quote?
(A) ₹1 = $0.0133
(B) ₹100 = £1.05
(C) € 1 = ₹85.00
(D) $1 = ₹75.00

Ans :

(D) $1 = ₹75.00
A direct quote is the home currency price for one unit of a foreign currency. For an Indian national, whose home currency is the Indian Rupee (₹), a quote like $1 = ₹75.00 is a direct quote because it states how many rupees are needed to buy one unit of the foreign currency (US Dollar).

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May/June 2010

12. What is an indirect quote in foreign exchange?
(A) The home currency price of one unit of the foreign currency.
(B) The foreign currency price of one unit of the home currency.
(C) A non-binding quote provided by a financial institution.
(D) A speculative quote that is estimated for a future date.

Ans :

(B) The foreign currency price of one unit of the home currency.
An indirect quote specifies the price of one unit of the home currency in terms of the foreign currency. For an Indian national, a quote like ₹1 = $0.0133 is an indirect quote because it expresses how many units of the foreign currency (US Dollar) can be acquired for one unit of the home currency (Indian Rupee).

Oct/Nov 2022

13. What is the mathematical relationship between a direct quote and an indirect quote?
(A) They are directly proportional to each other.
(B) They are always equal in value.
(C) They are reciprocals of each other.
(D) There is no defined mathematical relationship.

Ans :

(C) They are reciprocals of each other.
Direct and indirect quotes are mathematically inverse. The direct quote is equal to 1 divided by the indirect quote, and vice versa. For example, if the direct quote is 1 = ₹75, the corresponding indirect quote would be ₹1 = 1/75, which is approximately $0.0133. This reciprocal relationship allows for easy conversion between the two quoting conventions.

May/June 2005

14. Until 1st August 1993, what was the mandatory basis for banks in India to quote all foreign exchange rates?
(A) On a direct basis only, showing rupees per foreign unit.
(B) On a basis independently determined by each individual bank.
(C) On a flexible mix of direct and indirect bases depending on the currency.
(D) On an indirect basis only, showing foreign units per rupee.

Ans :

(D) On an indirect basis only, showing foreign units per rupee.
Before a significant change in market practice, banks in India were required to quote all foreign exchange rates on an indirect basis. This was the prevailing convention until 1st August 1993. Under this system, rates were expressed as the amount of foreign currency per one unit of the Indian Rupee.

Oct/Nov 2017

15. What change occurred in the Indian forex market's quoting convention from 2nd August 1993?
(A) Banks began quoting all rates on a direct basis only.
(B) Banks reverted to using both direct and indirect quotes.
(C) Banks were mandated to stop quoting rates altogether.
(D) Banks started quoting rates against a basket of currencies.

Ans :

(A) Banks began quoting all rates on a direct basis only.
A major shift in the Indian forex market occurred on 2nd August 1993. From this date onwards, banks in India moved away from the previous system of indirect quotations and began quoting all foreign exchange rates exclusively on a direct basis, expressing rates as the home currency price per unit of foreign currency.

May/June 2012

16. Statement (I): A direct quote is the foreign currency price of one unit of the home currency.
Statement (II): An indirect quote is the home currency price of one unit of the foreign currency.
Which of the following is correct?
(A) Both Statement (I) and Statement (II) are correct.
(B) Both Statement (I) and Statement (II) are incorrect.
(C) Statement (I) is correct, but Statement (II) is incorrect.
(D) Statement (I) is incorrect, but Statement (II) is correct.

Ans :

(B) Both Statement (I) and Statement (II) are incorrect.
Both statements misrepresent the definitions. A direct quote is the home currency price of one unit of the foreign currency (e.g., ₹75 / 1 for an Indian). An indirect quote is the foreign currency price of one unit of the home currency (e.g., 0.0133 / ₹1 for an Indian). The statements have the definitions reversed.

Oct/Nov 2009

17. In foreign exchange, what is a 'Cross Rate'?
(A) The historical exchange rate between a currency and a commodity like gold.
(B) An exchange rate derived from the rates of two currencies against a common third currency.
(C) The simple average of the daily buying and selling rates of a specific currency.
(D) A preferential exchange rate offered exclusively to central banks for official transactions.

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Ans :

(B) An exchange rate derived from the rates of two currencies against a common third currency. A cross rate is an exchange rate between two currencies that is calculated using their respective exchange rates against a common third currency, often the US dollar. This method is used when a direct quotation between the two desired currencies is not readily available in the market, allowing for an indirect calculation of their rate.

May/June 2023

18. If a banker in India needs to determine the Rupee/Euro exchange rate but it is not directly quoted, what is the typical procedure?
(A) First transact US Dollars against Rupees and then use those Dollars to acquire Euros.
(B) Estimate the rate based on historical trends and macroeconomic forecasts.
(C) Wait for the Reserve Bank of India to officially announce the rate for the day.
(D) Request that the customer make the payment in US Dollars directly to avoid conversion.

Ans :

(A) First transact US Dollars against Rupees and then use those Dollars to acquire Euros.
When a direct quote like Rupee/Euro is unavailable, a banker would use a cross rate calculation. The standard procedure involves using a widely traded intermediate currency, such as the US Dollar. The banker would first determine the cost of buying US Dollars with Rupees and then find the rate for selling those US Dollars to acquire Euros.

Oct/Nov 2018

19. Given the following rates: 1 = ₹74.8450/74.8545 and 1 = € 0.9027. What is the approximate rate for € 1 in Rupees for a person remitting Euros from India?
(A) ₹74.85
(B) ₹67.58
(C) ₹82.92
(D) ₹90.27

Ans :

(C) ₹82.92
To remit Euros, the person must first buy US Dollars and then sell those US Dollars to buy Euros. The cost to buy 1 is ₹74.8545. For 1, one gets € 0.9027. Therefore, the cost of € 1 is calculated as (Cost of in ₹) / (Euros per) = ₹74.8545 / 0.9027 ≈ ₹82.92.

May/June 2016

20. "If the rates in Mumbai market are $1 = ₹74.8450/545 and rates in London market are $1 = Euros 0.9027 we will get $1 for ₹74.8545 and for one US we will get Euro 0.9027."
In this context, why is the rate ₹74.8545 used in the calculation?
(A) It is the bank's selling rate for US, which is the customer's cost to buy US.
(B) It is the bank's buying rate for US$, representing the price the bank pays.
(C) It is the official inter-bank lending rate for Rupees set by the central bank.
(D) It is the specific rate at which the bank buys Euros in the international market.

Ans :

(A) It is the bank's selling rate for US, which is the customer's cost to buy US.
The two-way quote $1 = ₹74.8450/74.8545 represents the bank's buying and selling rates, respectively. To remit funds, a customer must buy the foreign currency (US$) from the bank. Therefore, the bank's selling rate (the higher rate), ₹74.8545, is applied, as this is the price the customer must pay to acquire one US Dollar.

Oct/Nov 2025

21. An Indian bank has to handle an export bill for £ 100,000 for a customer. The bank needs to purchase the Pound Sterling (£) and pay the customer in Rupees (₹). The prevailing inter-bank rates are 1 = ₹74.8450/74.8545 and £ 1 = 1.2720/1.2740. At what rate will the bank convert the customer's Pounds to Rupees?
(A) ₹95.4526 per £
(B) ₹95.3283 per £
(C) ₹95.2028 per £
(D) ₹95.0772 per £

Ans :

(C) ₹95.2028 per £
The bank is purchasing £ from the customer. It will sell these pounds in the international market at the market's buying rate for £, which is 1.2720. The US dollars obtained will then be sold (converted) in the local market at the market's buying rate for US, which is ₹74.8450. The cross rate is $1.2720 \times 74.8450 = 95.2028$.

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May/June 2019

50. "The formula is as follows: (Spot rate Interest rate differential Forward period) / (100 No. of days in the year)"
If the Spot rate and Forward period remain constant, what is the relationship between the Interest rate differential and the calculated Forward points?
(A) They are directly proportional.
(B) They are inversely proportional.
(C) There is no relationship between them.
(D) The relationship is exponential.

Ans :

(A) They are directly proportional.
According to the provided formula, the Interest Rate Differential is in the numerator. This means that if all other variables (Spot rate, Forward period, No. of days in the year) are held constant, an increase in the interest rate differential will lead to a proportional increase in the calculated forward points.

Oct/Nov 2006

51. What is another term for 'Forward differential'?
(A) Spot Rate
(B) Interest Rate
(C) Swap Rate
(D) Par Rate

Ans :

(C) Swap Rate
The forward differential, which is the difference between the forward rate and the spot rate, is also commonly known in the market as the 'Swap Rate' or 'swap points'. This term is used because these points are central to the pricing of forex swaps, which involve simultaneous spot and forward transactions.

May/June 2021

52. What is the formula for calculating the interest rate differential from the forward points?
(A) (Spot rate Forward period) / (Forward points No. of days in the year 100)
(B) (Forward points Spot rate 100) / (Forward period)
(C) (Spot rate Forward period 100) / (Forward points)
(D) (Forward points No. of days in the year 100) / (Spot rate Forward period)

Ans :

(D) (Forward points No. of days in the year 100) / (Spot rate Forward period)
To find the annualized interest rate differential implied by the forward points, one must rearrange the formula for calculating forward points. The correct formula multiplies the forward points by the number of days in the year and 100, then divides by the product of the spot rate and the forward period.

NODIA

Oct/Nov 2010

53. An analyst observes the following data: Forward points = 0.01125, Spot rate = 1.50, Forward period = 90 days, and the year is assumed to have 360 days. What is the annualized interest rate differential?
(A) 2.5% per annum
(B) 3.5% per annum
(C) 3.0% per annum
(D) 4.0% per annum

Ans :

(C) 3.0% per annum
Using the formula: Interest rate differential = (Forward points No. of days 100) / (Spot rate Forward period). Plugging in the values: (0.01125 360 100) / (1.50 90) = 405 / 135 = 3. This result represents an annualized interest rate differential of 3% per annum.

May/June 2005

54. The difference between the spot exchange rate and the forward exchange rate is known as what?
(A) The interest differential
(B) The spot margin
(C) The rate spread
(D) The forward differential

Ans :

(D) The forward differential
The forward differential is explicitly defined as the difference between the spot rate and the forward rate for a given currency pair and tenor. This differential, which can be positive (premium) or negative (discount), reflects the cost of carry, primarily driven by the interest rate difference between the two currencies.

Oct/Nov 2022

55. If the spot rate for $1 is ₹74.8450 and the 3-months forward rate is ₹74.8725, what can be concluded?
(A) The US is at a premium vis-à-vis the rupee.
(B) The US is at a discount vis-à-vis the rupee.

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working day following the date on which the deal was concluded.

Oct/Nov 2021

27. What is the standard settlement period for a 'Spot' transaction in the foreign exchange market?
(A) The same day as the deal is concluded.
(B) The next working day after the deal is concluded.
(C) Thirty calendar days after the date of the deal.
(D) The second working day after the date of the deal.

Ans :

(D) The second working day after the date of the deal.
A 'Spot' transaction is the most common type of forex deal. The spot rate is the exchange rate for a transaction where settlement, the actual exchange of currencies, is set to occur on the second working day after the deal has been agreed upon. This is often denoted as T+2 settlement.

May/June 2024

28. A 'Forward rate' applies to a transaction where the exchange of currencies takes place at what time?
(A) On a date after the standard spot settlement date.
(B) On the same day that the deal is originally agreed upon.
(C) On the next working day immediately after the deal.
(D) On the second working day after the deal is agreed upon.

Ans :

(A) On a date after the standard spot settlement date.
A forward rate is the exchange rate for a transaction where the value date is any date beyond the standard spot settlement date (T+2). These rates are used for locking in a price for a future currency exchange and are typically expressed by indicating a premium or discount over the spot rate.

Oct/Nov 2016

29. Statement (A): The TOM rate is for a transaction settling on the second working day after the deal date.
Reason (R) : The SPOT rate is for a transaction settling on the next working day after the deal date.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) Both (A) and (R) are false.

Ans :

(D) Both (A) and (R) are false.
Both the assertion and the reason are incorrect. The TOM (tomorrow) rate is for a transaction settling on the next (first) working day after the deal date. The SPOT rate is for a transaction settling on the second working day after the deal date. The statements have reversed the definitions of TOM and SPOT settlement periods.

May/June 2009

30. When is a currency said to be at a 'premium' in the forward market?
(A) When it is costlier to acquire for a future value date compared to the spot market.
(B) When it is cheaper to acquire in the forward market compared to the spot market.
(C) When its forward exchange rate is exactly the same as its current spot rate.
(D) When the currency is only available for spot transactions and not for forward delivery.

Ans :

(A) When it is costlier to acquire for a future value date compared to the spot market.
A currency is considered to be at a premium when its forward rate is higher than its spot rate, meaning it is more expensive to buy for a future settlement date. In the case of direct quotations, this premium is added to both the buying and selling spot rates to arrive at the forward rates.

Oct/Nov 2020

31. If a currency is at a 'discount' for a future value date, what does this imply?
(A) The currency is more expensive to acquire in the forward market.
(B) The currency's exchange rate is expected to be highly stable.
(C) The forward market for that specific currency is currently closed.
(D) The currency is cheaper to acquire in the forward market.

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Oct/Nov 2013

41. The determination of forward points based on interest rate differentials is based on a trade-off between what two elements?

(A) The risk of currency fluctuation and the political stability of the government.
(B) The transaction cost of the spot deal and the cost of the forward deal.
(C) The inflation rate in one country and the unemployment rate in the other.
(D) The interest earned on one currency and the opportunity foregone to earn interest on another.

Ans :

(D) The interest earned on one currency and the opportunity foregone to earn interest on another. The logic behind using interest rate differentials to determine forward points is the concept of a financial trade-off. It balances the interest income that can be generated by holding one currency against the opportunity cost of not holding the other currency and earning interest on it. The forward rate adjusts to equalize these returns.

May/June 2008

42. Consider the following cash flow table for a transaction involving borrowing Euro, converting to US$, and investing the US$:

Transaction	Euro Inflow	Euro Outflow	US Inflow	US Outflow
Spot borrowing	+100	–	–	–
Sells Euros	–	-100	+150	–
One year hence interest	–	-3	+9	–
Total	–	-103	+159	–

What does the inflow of "+150" in the US column signify?

(A) The principal amount of US received from converting the borrowed € 100 at the spot rate.
(B) The total interest earned on the US deposit after the full one-year period.
(C) The total US amount, including both principal and interest, at the end of the year.
(D) A net arbitrage gain of $150 realized from the entire transaction at its inception.

Ans :

(A) The principal amount of US received from converting the borrowed € 100 at the spot rate.
The table illustrates a transaction starting with borrowing € 100. The "Sells Euros" line shows an outflow of 100 from the Euro column and a corresponding inflow into the US column. Given a spot rate of € 1 = $1.5000, selling € 100 results in receiving $150. This "+150" is the initial US dollar principal obtained from the conversion.

Oct/Nov 2009

43. An investor borrows € 100 for one year at 3% p.a. and converts it to US at a spot rate of € 1 = 1.5000. The US are then deposited for one year at 6% p.a. If the one-year forward exchange rate is also € 1 = 1.5000, what is the investor's net gain in Euros?

(A) € 6
(B) € 9
(C) There is no net gain.
(D) € 3

Ans :

(D) € 3
After one year, the investor owes € 103 (100 principal + 3 interest). The US deposit grows to 159 (150 principal + 9 interest). Converting 159 back to Euros at the rate of 1.5000 per Euro gives 159 / 1.5000 = € 106. The net gain is the amount received (€ 106) minus the amount owed (€ 103), which equals € 3.

NODIA

May/June 2023

44. To eliminate the arbitrage opportunity in the previous question, what should the one-year forward rate of US$/Euro be?

(A) 1.5000
(B) 1.5436
(C) 1.4563
(D) 1.5300

Ans :

(B) 1.5436
To eliminate arbitrage, the returns in both currencies must be equal. At the end of the year, the investor owes € 103 and holds 159. The forward rate must be such that 159 exactly equals € 103. Therefore, the no-arbitrage forward rate is € 1 = 159 / 103, which is approximately 1.5436.

Oct/Nov 2018

45. What does the difference between the no-arbitrage forward rate (e.g., 1.5436) and the spot rate (e.g., 1.5000) represent?

(B) Spot basis (T+2)
(C) TOM basis (T+1)
(D) Forward basis (T+30)

Ans :

(B) Spot basis (T+2)
While various settlement dates exist, the standard market convention is to quote exchange rates on a spot basis. This means the default settlement for a quoted rate is the second working day after the transaction date (T+2). Rates for other value dates like cash, tom, or forward are derived from this spot rate.

Oct/Nov 2005

37. A forward exchange rate is composed of which two components?
(A) The previous day's closing rate and a market sentiment index.
(B) The central bank's official reference rate and a specific risk premium.
(C) The opening rate of the day and the closing rate of the day.
(D) The current spot rate and the relevant forward points (differential).

Ans :

(D) The current spot rate and the relevant forward points (differential).
A forward rate is not quoted as a standalone figure but is derived from two key components. The first is the current spot exchange rate. The second is the forward points (also known as forward differential or swap points), which represent the adjustment for the interest rate differential between the two currencies for the forward period.

May/June 2020

38. If the spot rate for € 1 is 1.2180 and the three-months forward rate is € 1 = 1.2330, what are the forward points?
(A) 150 points
(B) 1.2330 points
(C) 1.2180 points
(D) -150 points

Ans :

(A) 150 points
The forward points represent the difference between the forward rate and the spot rate. The difference is calculated as Forward Rate - Spot Rate = 1.2330 - 1.2180 = 0.0150. In market terminology, this difference is referred to as 150 points. Since the forward rate is higher, these points represent a premium on the Euro.

Oct/Nov 2023

39. Which of the following is NOT a factor that determines forward points?
(A) Supply and demand for the currency for the specific future settlement date.
(B) Market expectations about future interest rates and foreign exchange movements.
(C) The historical spot rate from the corresponding period in the previous year.
(D) The interest rate differential between the two countries' currencies for the period.

Ans :

(C) The historical spot rate from the corresponding period in the previous year.
Forward points are determined by future-oriented factors. These include the specific supply and demand dynamics for the forward settlement date, market views on future developments, and most importantly, the interest rate differential between the currencies. The historical spot rate from a year ago is not a direct determinant of current forward points.

May/June 2006

40. In a market with no controls on capital flows, what is considered the most dominant factor in determining forward points?
(A) The interest rate differential between the two currencies.
(B) The balance of trade figures between the two countries.
(C) The comparative political stability of the two countries.
(D) The daily trading volume and liquidity of the currencies.

Ans :

(A) The interest rate differential between the two currencies.
While supply/demand and market expectations play a role, the interest rate differential between the two currencies is the most dominant factor determining forward points in a free market. This is based on the principle of interest rate parity, which links forward rates to the difference in interest that can be earned on the two currencies.

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May/June 2018

22. What is the 'thumb rule of the market' regarding price quotations?

(A) The quoting party must always accept any reasonable counter-offer from the client.

(B) The quoting party provides a price, and the other party can either accept the deal or not.

(C) The client who requests the quote has the right to dictate the prices at which they wish to deal.

(D) Prices quoted by a bank are considered binding for the entire trading day without any change.

Ans :

(B) The quoting party provides a price, and the other party can either accept the deal or not.

The market's thumb rule states that the party asking for a quote is the price taker, not the price maker. The quoting party will provide their bid and offer prices, and it is up to the requesting party to decide whether to transact at those prices. They cannot dictate the prices but can always ask for a fresh quote.

Oct/Nov 2014

23. The 'Chain Rule' in forex arithmetic is a method used for what purpose?

(A) To calculate the accrued interest on foreign currency deposits over time.

(B) To set the official value date for a standard spot transaction.

(C) To determine the cross rate between two currencies via a third currency.

(D) To forecast the direction of future exchange rates using technical analysis.

Ans :

(C) To determine the cross rate between two currencies via a third currency.

The Chain Rule is a systematic approach used to calculate a cross exchange rate. It formalizes the common-sense method of linking the exchange rates of two currencies through a third, common currency to find the rate between the original pair. It is essentially the underlying principle for cross rate calculations.

May/June 2021

24. What is the 'Value Date' in a foreign exchange transaction?

(A) The date on which the deal is initially agreed upon by the two parties.

(B) The date on which the formal contract for the deal is signed and documented.

(C) The final date by which a transaction can be cancelled without incurring a penalty.

(D) The date on which the actual exchange of currencies between parties takes place.

Ans :

(D) The date on which the actual exchange of currencies between parties takes place.

The value date is a critical concept in foreign exchange, representing the specific date on which the actual settlement of the transaction occurs. This is the day the two parties involved in the deal exchange the currencies they have agreed to trade, fulfilling their respective obligations and completing the transaction.

Oct/Nov 2010

25. An exchange of currencies that takes place on the same day as the deal is known as which type of rate?

(A) SPOT rate

(B) TOM rate

(C) Cash/Ready rate

(D) Forward rate

Ans :

(C) Cash/Ready rate

A Cash/Ready rate applies when the exchange of currencies, or settlement, occurs on the very same day that the transaction is agreed upon. This provides the quickest settlement, with funds in the respective currencies being exchanged between the parties' accounts before the end of the business day of the deal.

May/June 2013

26. If the exchange of currencies is scheduled for the next working day after the deal is made, what is the transaction rate called?

(A) Spot rate

(B) Tom rate

(C) Ready rate

(D) Cash rate

Ans :

(B) Tom rate

The term 'Tom rate' is short for 'tomorrow rate'. It refers to the exchange rate for a transaction where the settlement, or the actual exchange of currencies, is scheduled to take place on the next

NODIA

(A) The forward differential.
(B) The transaction cost.
(C) The spot differential.
(D) The interest rate spread.

Ans :

(A) The forward differential.
The difference between the forward exchange rate and the spot exchange rate is known as the forward differential or forward points. In the example, this difference is 1.5436 - 1.5000 = 0.0436. This differential reflects the adjustment required to compensate for the interest rate difference between the two currencies over the forward period.

May/June 2007

46. What is 'Arbitrage' in the context of financial markets?
(A) A long-term investment strategy based on fundamental economic forecasts.
(B) The act of making risk-free profits by undertaking offsetting transactions.
(C) A government policy designed to control and stabilize exchange rates.
(D) The process of borrowing funds directly from a country's central bank.

Ans :

(B) The act of making risk-free profits by undertaking offsetting transactions.
Arbitrage is an operation where one can achieve a guaranteed, risk-free profit by exploiting price differences. This involves undertaking offsetting transactions, such as borrowing a currency at a low interest rate in one centre and lending it at a higher rate in another, or buying and selling a currency simultaneously in different markets.

Oct/Nov 2025

47. Why are arbitrage opportunities considered very rare in today's foreign exchange markets?
(A) Due to strict international government regulations that explicitly prohibit them.
(B) Due to the prohibitively high transaction costs involved in cross-market trades.
(C) Due to the general lack of significant interest rate differentials between countries.
(D) Due to the high speed and efficiency of modern communication systems.

Ans :

(D) Due to the high speed and efficiency of modern communication systems.
Modern financial markets are characterized by highly efficient communication and information systems. Price discrepancies between markets are identified and acted upon almost instantaneously by traders. This rapid action quickly eliminates any arbitrage opportunities, making them very rare and short-lived in the forex market.

May/June 2012

48. I. Arbitrage involves making risk-free profits.
II. Arbitrage can occur in interest rates by borrowing at one centre and lending at another at a higher rate.
III. Arbitrage opportunities are common due to slow communication systems.
Which of the statements is/are correct?
(A) Only I
(B) Only I and II
(C) Only II and III
(D) I, II, and III

Ans :

(B) Only I and II
Statements I and II correctly define arbitrage and provide a valid example. Arbitrage is indeed about making risk-free profits from price discrepancies, and interest rate arbitrage is a classic example. However, statement III is incorrect; arbitrage opportunities are very rare in modern markets precisely because of efficient, not slow, communication systems.

Oct/Nov 2014

49. Using the formula for calculating approximate forward points, what are the forward points for a 90-day period given a spot rate of 1.5000, an interest rate differential of 3% p.a., and a 360-day year?
(A) 0.01500
(B) 0.01125
(C) 0.03000
(D) 0.04500

Ans :

(B) 0.01125
The formula is Forward Points = (Spot rate Interest rate differential Forward period) / (100 No. of days in the year). Plugging in the values: (1.5000 3 90) / (100 360) = 405 / 36000 = 0.01125. These are the approximate forward points for the 90-day period.

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Ans :

(A) The spot rate is adjusted for the forward points for three months.
The method to arrive at an outright forward rate is to take the current spot rate and adjust it using the forward points corresponding to the desired forward period. For a three-month forward rate, the three-month forward points are either added to (for a premium) or subtracted from (for a discount) the spot rate.

Oct/Nov 2019

61. "Let us consider US$/Euro rate
Spot € 1 = $1.2180/1.2190
The currency which is being bought and sold is the Euro in terms of US. The bid rate for Euro is 1.2180 whereas the offer rate is 1.2190."
Based on this information, at what price can a customer buy Euros from the bank?
(A) 1.2180
(B) The average of 1.2180 and 1.2190.
(C) 1.2190
(D) A rate specially negotiated with the bank.

Ans :

(C) 1.2190
The quote 1.2180/90 represents the bank's bid/offer rates. The bid rate (1.2180) is the price at which the bank buys the base currency (Euro). The offer rate (1.2190) is the price at which the bank sells the base currency. Therefore, a customer wanting to buy Euros must pay the bank's offer rate of $1.2190.

May/June 2009

62. Given the quotation:
Spot € 1 = 1.2180/1.2190
Forward differentials 2 month = 30-37
What do these forward differentials indicate about the base currency, the Euro?
(A) The Euro is at a discount because 30 is less than 37.
(B) The Euro is at a premium because the first figure (30) is lower than the second figure (37).
(C) The Euro is at a premium because the points are positive numbers.
(D) The Euro is at a discount because the points are applied to the US$.

Ans :

(B) The Euro is at a premium because the first figure (30) is lower than the second figure (37).
The convention for interpreting forward points is that if the first figure is lower than the second figure (ascending order, e.g., 30-37), the base currency is at a premium. In this quote, the base currency is the Euro. Therefore, the Euro is at a premium for the two-month forward period.

Oct/Nov 2011

63. A bank provides the following quote: Spot € 1 = 1.2180/1.2190 and 2-month forward differentials are 30-37. A corporate treasurer wants to buy Euros two months forward. What is the outright rate per Euro that the bank will quote?
(A) 1.2227
(B) 1.2210
(C) 1.2217
(D) 1.2150

Ans :

(A) 1.2227
The treasurer wants to buy Euros, so the bank's offer rate applies. The spot offer rate is 1.2190. The forward points (30-37) indicate a premium, so they are added. The offer side points are the higher number, 37. The outright forward offer rate is 1.2190 + 0.0037 = 1.2227.

May/June 2010

64. Using the same quote (Spot € 1 = $1.2180/1.2190, 2-month forward 30-37), an exporter wants to sell Euros to the bank for 2-month forward delivery. What outright rate will the bank apply?
(A) 1.2227
(B) 1.2150
(C) 1.2143
(D) 1.2210

Ans :

(D) 1.2210
The exporter is selling Euros, so the bank's buying (bid) rate applies. The spot bid rate is 1.2180. The forward points (30-37) indicate a premium (added). The bid side points are the lower number, 30. The outright forward bid rate is 1.2180 + 0.0030 = 1.2210.

Oct/Nov 2024

65. Consider the quotation:
Spot Rate € 1 = 1.2180/1.2190
1 month forwards = 24-19
What does this set of forward differentials signify?

NODIA

(C) The rupee is at a premium vis-à-vis the US$.
(D) The forward market is at par.

Ans :

(A) The US is at a premium vis-à-vis the rupee.
The forward rate (₹74.8725) is higher than the spot rate (₹74.8450). This means the US dollar is costlier to buy in the three-month forward market compared to the spot market. Therefore, the US dollar is said to be at a premium against the Indian rupee for this forward period.

May/June 2018

56. An importer needs to buy US three months forward. The spot rate for 1 is ₹74.8450 and the 3-months forward rate is ₹74.8725. How much more does the importer have to pay per US for the forward purchase compared to a spot purchase?
(A) ₹0.0500
(B) ₹0.0275
(C) ₹0.0748
(D) The importer pays less.

Ans :

(B) ₹0.0275
The cost of buying US in the spot market is ₹74.8450. The cost of buying US three months forward is ₹74.8725. The additional amount the importer has to pay is the difference between the forward rate and the spot rate, which is ₹74.8725 - ₹74.8450 = ₹0.0275 per US dollar.

Oct/Nov 2016

57. In the case of direct quotations, how is a premium treated when calculating the forward rate?
(A) It is deducted from the buying side and added to the selling side.
(B) It is deducted from both the buying and selling side.
(C) It is added to the buying side and deducted from the selling side.
(D) It is added to both the buying and selling side.

Ans :

(D) It is added to both the buying and selling side.
For direct quotations, when a currency is at a premium, the forward points representing that premium are always added. This addition is performed on both the buying (bid) rate and the selling (offer) rate of the spot quote to arrive at the outright forward bid and offer rates.

May/June 2014

58. If the spot rate for $1 is ₹74.8450 and the 3-months forward rate is ₹74.7950, what does this indicate?
(A) The US is at a discount of ₹0.0500.
(B) The US is at a premium of ₹0.0500.
(C) The rupee is at a discount of ₹0.0500.
(D) The market is inefficient.

Ans :

(A) The US is at a discount of ₹0.0500.
The forward rate (₹74.7950) is lower than the spot rate (₹74.8450). This means the US dollar is cheaper to buy in the three-month forward market. The difference is ₹74.8450 - ₹74.7950 = ₹0.0500. Therefore, the US dollar is at a discount of ₹0.0500 against the Indian rupee.

Oct/Nov 2007

59. According to foreign exchange market convention, how are forward rates typically quoted?
(A) As a single, all-inclusive outright rate for each separate forward period.
(B) By providing a percentage increase or decrease from the previous day's close.
(C) By quoting the current spot rate and the forward differentials separately.
(D) As a wide range of possible future rates based on volatility forecasts.

Ans :

(C) By quoting the current spot rate and the forward differentials separately.
The standard market convention is not to quote full outright forward rates for various tenors. Instead, dealers quote the current spot rate along with a separate set of forward differentials (or points) for different periods like one, two, or three months. The outright forward rate is then calculated by adjusting the spot rate with these points.

May/June 2025

60. To derive the forward rate for three months, what adjustment is made?
(A) The spot rate is adjusted for the forward points for three months.
(B) The one-month forward rate is simply multiplied by three.
(C) The average of the spot rate and the expected future spot rate is taken.
(D) The spot rate is ignored, and only the three-month forward points are used.

NODIA

Ans :

(D) The currency is cheaper to acquire in the forward market.
A currency is at a discount when its forward rate is lower than its spot rate. This indicates that the currency is cheaper to acquire for a future value date compared to immediate (spot) settlement. For direct quotations, the discount amount is subtracted from both the spot buying and selling rates to determine the forward rates.

May/June 2011

32. In the case of a direct quotation, how is a premium or discount applied to the spot rate to calculate the forward rate?
(A) Premium is subtracted from the spot rate and discount is added to it.
(B) Premium is added to the spot rate and discount is subtracted from it.
(C) Both premium and discount are always added to the spot rate.
(D) Both premium and discount are always subtracted from the spot rate.

Ans :

(B) Premium is added to the spot rate and discount is subtracted from it.
When using the direct method of quotation, a forward premium is always added to the spot rate to calculate the higher forward rate. Conversely, a forward discount is always subtracted from the spot rate to calculate the lower forward rate. This adjustment applies to both the buying (bid) and selling (offer) sides of the quote.

Oct/Nov 2012

33. "For example: Spot € 1 = $1.2180/1.2190, 1 month forward 35-32, 2 month forward 72-70, 3 month forward 110-107"
Based on this data, what can be concluded about the Euro for forward dates?
(A) The Euro is at a premium against the US$.
(B) The Euro is at a discount against the US$.
(C) The Euro is at par with the US$.
(D) The US is at a discount against the Euro.

Ans :

(B) The Euro is at a discount against the US$.
The forward points are quoted with the first number being higher than the second (e.g., 35-32, 72-70). This convention indicates that the base currency, which is the Euro in this quote, is at a discount. Consequently, the discount points are subtracted from the spot rate to calculate the outright forward rates.

May/June 2015

34. Using the forward rate quotation 'Spot € 1 = $1.2180/1.2190' and '1 month forward 35-32', what is the outright rate to sell € 1 for one-month forward delivery?
(A) $1.2145
(B) $1.2148
(C) $1.2215
(D) $1.2222

Ans :

(A) $1.2145
To sell € 1, we use the bank's buying rate (bid rate), which is 1.2180. The forward points for the bid side are the first number, 35. Since the points (35-32) indicate a discount, we subtract.
The outright forward bid rate is
1.2180 - 0.0035 = 1.2145.
The bank will buy 1 Euro at $1.2145 for one-month forward delivery.

Oct/Nov 2007

35. If a currency is at a premium vis-à-vis another currency, what is the natural consequence for the second currency?
(A) It will be at a discount vis-à-vis the first currency.
(B) It will also be at a premium against the first currency.
(C) It will be at par with the first currency.
(D) Its exchange rate value will become highly unstable.

Ans :

(A) It will be at a discount vis-à-vis the first currency.
The relationship between premium and discount is reciprocal. If one currency is at a premium (costlier in the forward market) compared to another, it logically follows that the second currency must be at a discount (cheaper in the forward market) relative to the first. Both cannot be at a premium simultaneously.

May/June 2017

36. What is the most common basis on which foreign exchange rates are generally quoted for settlement?
(A) Cash basis (T+0)

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(A) The base currency, Euro, is at a premium.
(B) The US Dollar is at a discount.
(C) The forward market is at par.
(D) The base currency, Euro, is at a discount.

Ans :

(D) The base currency, Euro, is at a discount.
The rule for interpreting forward points states that if the first figure is higher than the second figure (descending order, e.g., 24-19), the base currency is at a discount. In this quotation, the base currency is the Euro. Therefore, these forward points indicate that the Euro is at a discount for the one-month forward period.

May/June 2017

66. When a currency is at a discount, how are the forward points applied to the spot rate?
(A) They are added to the bid rate and subtracted from the offer rate.
(B) They are always added to both the bid and offer rates.
(C) They are always deducted from both the bid and offer rates.
(D) They are subtracted from the bid rate and added to the offer rate.

Ans :

(C) They are always deducted from both the bid and offer rates.
When the forward points indicate that the base currency is at a discount, the points are always deducted (subtracted) from the spot rates. This deduction is applied to both the bid (buying) rate and the offer (selling) rate to calculate the respective outright forward rates, resulting in a wider bid-offer spread.

Oct/Nov 2005

67. If forward points for a discount are 26-20, which value is deducted from the bid rate and which from the offer rate?
(A) 26 is deducted from the offer rate, and 20 is deducted from the bid rate.
(B) 20 is deducted from the bid rate, and 26 is deducted from the offer rate.
(C) The higher point (26) is deducted from the bid rate, and the lower point (20) is deducted from the offer rate.
(D) The average of 26 and 20 is deducted from both rates.

Ans :

(C) The higher point (26) is deducted from the bid rate, and the lower point (20) is deducted from the offer rate.
To maintain the bid-offer spread, the larger discount amount must be applied to the bid rate (making it lower), and the smaller discount amount must be applied to the offer rate. Therefore, the higher forward point (26) is deducted from the bid rate, and the lower forward point (20) is deducted from the offer rate.

May/June 2020

68. A bank quotes: Spot € 1 = 1.2180/1.2190, with 2-month forward points of 26-20. What is the 2-month outright bid rate for Euro?
(A) 1.2154
(B) 1.2160
(C) 1.2170
(D) 1.2206

Ans :

(A) 1.2154
The spot bid rate is 1.2180. The forward points (26-20) indicate a discount, so they must be subtracted. For the bid rate, the higher point (26) is used. The calculation is: 1.2180 - 0.0026 = 1.2154. This is the outright 2-month forward bid rate for one Euro.

Oct/Nov 2023

69. Given the same quote: Spot € 1 = 1.2180/1.2190, with 2-month forward points of 26-20. What is the 2-month outright offer rate for Euro?
(A) 1.2160
(B) 1.2154
(C) 1.2170
(D) 1.2210

Ans :

(C) 1.2170
The spot offer rate is 1.2190. The forward points (26-20) indicate a discount, which must be subtracted. For the offer rate, the lower point (20) is used. The calculation is: 1.2190 - 0.0020 = 1.2170. This is the outright 2-month forward offer rate for one Euro.

May/June 2006

70. Based on the calculations in the previous two questions, what is the 2-month outright forward quote for € 1?
(A) 1.2154 - 1.2170
(B) 1.2154 - 1.2160

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the interest rate differential is 2.5% p.a., and the bank uses a 360-day year. The approximate forward points would be:
(A) 0.009375
(B) 0.033750
(C) 0.005625
(D) 0.002500

Ans :

(C) 0.005625
Using the formula: Forward Points = (Spot rate Interest rate differential Forward period) / (100 No. of days in the year). Calculation: (1.3500 2.5 60) / (100 360) = 202.5 / 36000 = 0.005625. These are the approximate forward points for the 60-day period.

May/June 2017

100. The concept that in an efficient market, the forward exchange rate should be set such that it prevents any risk-free profit from interest rate differentials is known as:
(A) Interest Rate Parity
(B) Purchasing Power Parity
(C) The Fisher Effect
(D) The Law of One Price

Ans :

(A) Interest Rate Parity
Interest Rate Parity (IRP) is a key theory in international finance that describes the relationship between interest rates and currency exchange rates. It posits that the forward premium or discount on a currency should be equal to the interest rate differential between the two countries, thereby eliminating any arbitrage opportunities.

Oct/Nov 2005

101. If a bank in India quotes a direct rate for USD, what does it represent?
(A) The number of US Dollars required to buy one Indian Rupee.
(B) The specific interest rate on a US Dollar deposit account in India.
(C) The number of Euros required to buy one US Dollar in the global market.
(D) The number of Indian Rupees required to buy one US Dollar.

Ans :

(D) The number of Indian Rupees required to buy one US Dollar.
A direct quote is the home currency price of one unit of foreign currency. For a bank in India, the home currency is the Indian Rupee (INR). Therefore, a direct quote for the US Dollar (USD) will be expressed as the number of INR needed to purchase one USD (e.g., ₹75.00/$1).

May/June 2020

102. What was the significance of August 2, 1993, in the Indian foreign exchange market?
(A) The Rupee was made fully convertible on the capital account, allowing free capital flows.
(B) Banks in India switched from the convention of indirect to direct quotation of exchange rates.
(C) The Liberalised Exchange Rate Management System (LERMS) was officially abolished.
(D) The RBI ceased all intervention and management of its foreign exchange reserves.

Ans :

(B) Banks in India switched from the convention of indirect to direct quotation of exchange rates.
August 2, 1993, marked a significant operational change in the Indian forex market. On this date, banks moved away from the practice of quoting rates on an indirect basis (foreign currency per INR 1) and adopted the international convention of quoting on a direct basis (INR per 1 unit of foreign currency).

Oct/Nov 2023

103. "The thumb rule of the market is that if you ask for a quote, the quoting party will give you a quote and it is for you to do the deal or not to do a deal on the prices quoted. You cannot dictate prices." This rule establishes which party as the 'price taker'?
(A) The party quoting the price.
(B) The central bank.
(C) The party asking for the quote.
(D) The broker facilitating the deal.

Ans :

(C) The party asking for the quote.
The thumb rule clearly indicates that the party providing the quote is the 'price maker', as they set the bid and offer rates. The party that requests the quote must then decide whether to accept these prices. This makes the party asking for the quote the 'price taker' in the transaction.

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(B) Almost every country has its own distinctive unit of account or currency.
(C) Currency exchanges are mostly put through by banks using bookkeeping entries.
(D) Almost all currency exchanges are effected with the help of credit instruments.

Ans :

(A) The useful possession of a currency is easily transferable and valid in any country.
A fundamental aspect of foreign exchange is that a country's currency (legal tender) is normally only useful within that specific country. It is not easily transferable or valid for transactions in other countries, which is the very reason the mechanism of foreign exchange is necessary for international trade and finance.

May/June 2022

76. Match List-I (Value Date Type) with List-II (Settlement Period).
List-I
P. Cash Rate
Q. TOM Rate
R. Spot Rate
S. Forward Rate
List-II
1. Second working day after the deal
2. After the spot date
3. Same day as the deal
4. Next working day after the deal
Code:
(A) P-3, Q-4, R-1, S-2
(B) P-1, Q-2, R-3, S-4
(C) P-3, Q-1, R-4, S-2
(D) P-4, Q-3, R-2, S-1

Ans :

(A) P-3, Q-4, R-1, S-2
Cash/Ready rate settles on the same day (P-3). TOM rate settles on the next working day (Q-4). Spot rate settles on the second working day after the deal (R-1). Forward rate settles on any date after the spot date (S-2). This matching correctly aligns each rate type with its standard settlement period.

Oct/Nov 2012

77. Which of the following factors is considered the most dominant in determining forward points in a market without capital controls?
(A) Political forecasts and election outcomes.
(B) Historical exchange rate volatility data.
(C) The total volume of speculative trading.
(D) The interest rate differential between the currencies.

Ans :

(D) The interest rate differential between the currencies.
While market sentiment and supply/demand play a role, the primary driver of forward points in a free market is the interest rate differential. The principle of interest rate parity dictates that the forward premium or discount should offset the difference in interest rates between the two currencies to prevent risk-free arbitrage opportunities.

May/June 2015

78. I. A direct quote for an Indian is $1 = ₹75.
II. An indirect quote for an Indian is ₹1 = 0.0133.
III. From August 2, 1993, Indian banks began quoting on a direct basis only.
IV. Direct and indirect quotes are independent of each other.
Which combination of statements is correct?
(A) I, II, III, and IV
(B) I, II, and III only
(C) II and IV only
(D) I and III only

Ans :

(B) I, II, and III only
Statements I, II, and III are all factually correct. Statement I is a correct example of a direct quote. Statement II is a correct example of an indirect quote. Statement III correctly states the historical change in quoting convention in India. Statement IV is incorrect because direct and indirect quotes are reciprocals of each other.

Oct/Nov 2021

79. **Assertion (A) :** In a direct quote, a forward premium is added to the spot rate to find the forward rate.
Reason (R) : A premium means the base currency is costlier in the forward market than in the spot market.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

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lower than the spot rate.
(C) An exporter selling USD three months forward will receive more rupees than at spot.
(D) The forward points for the period are negative and must be subtracted.

Ans :

(C) An exporter selling USD three months forward will receive more rupees than at spot.
A premium on the USD means the forward rate (INR per USD) is higher than the spot rate. For an exporter selling USD, the bank's buying rate will be higher in the forward market than the spot market. Therefore, the exporter will receive more rupees for each dollar sold forward.

May/June 2019

110. Match List-I (Concept) with List-II (Description).
List-I
P. Direct Quote
Q. Forward Rate
R. Arbitrage
S. Cross Rate
List-II
1. Rate derived via a third currency
2. Risk-free profit
3. Home currency per unit of foreign currency
4. Rate for settlement beyond T+2
Code:
(A) P-1, Q-2, R-3, S-4
(B) P-3, Q-4, R-2, S-1
(C) P-3, Q-2, R-4, S-1
(D) P-4, Q-3, R-1, S-2

Ans :

(B) P-3, Q-4, R-2, S-1
A Direct Quote is the home currency price per unit of foreign currency (P-3). A Forward Rate is for settlement after the spot date (Q-4). Arbitrage is the opportunity for risk-free profit (R-2). A Cross Rate is a rate derived using a third currency (S-1). This matching correctly aligns the concepts.

Oct/Nov 2008

111. The settlement of a foreign exchange transaction is effected by which of the following means?
(A) Primarily through the physical delivery of cash via international armored transport.
(B) Through the direct issuance of sovereign bonds from one government to another.
(C) By exchanging equivalent amounts of gold bullion stored in central bank vaults.
(D) By means of bookkeeping entries in the respective correspondent bank accounts.

Ans :

(D) By means of bookkeeping entries in the respective correspondent bank accounts.
The vast majority of foreign exchange settlements are conducted through electronic bookkeeping. Banks in the respective countries make corresponding debit and credit entries in the accounts they hold with each other (correspondent accounts). This system is efficient and avoids the risks associated with physically moving large sums of money across borders.

May/June 2022

112. "Calculation of the cross rate is based on a common sense approach. However, it can be reduced to a rule known as the chain rule with similar steps."
This implies that the Chain Rule is a:
(A) Completely different and more complex method than cross rate calculation.
(B) A formalized, step-by-step procedure for what is an intuitive calculation.
(C) A method that is used only when the common sense approach fails to yield a result.
(D) A simplified version of cross rate calculation that is generally less accurate.

Ans :

(B) A formalized, step-by-step procedure for what is an intuitive calculation.
The text suggests that calculating a cross rate is fundamentally a "common sense" process. It then introduces the Chain Rule as a way to structure this process into a defined rule with specific steps. Therefore, the Chain Rule is not a different method but rather a more formal and systematic way to perform the cross rate calculation.

Oct/Nov 2011

113. If Euro is at a discount vis-a-vis the US Dollar, then the US Dollar is at a _____ vis-a-vis the Euro.
(A) discount
(B) par
(C) premium
(D) variable rate

Ans :

(C) premium

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(D) Spot transaction
By definition, a spot transaction in the foreign exchange market is one where the settlement, or value date, is scheduled for the second business day following the date on which the transaction was agreed upon. This T+2 settlement is the standard convention for most foreign exchange dealings.

Oct/Nov 2025

85. If forward points are quoted as 50-45, what does this imply for the base currency?
(A) It is at a discount because the first number is higher than the second.
(B) It is at a premium because the numbers are positive values.
(C) It is at a premium because the second number is lower than the first.
(D) It is at par because the difference between the points is small.

Ans :

(A) It is at a discount because the first number is higher than the second.
The market convention for interpreting forward points is that if they are quoted in descending order (e.g., 50-45), the base currency is at a discount. The discount points are then subtracted from the spot rate to calculate the outright forward rate, with the larger number being subtracted from the bid price.

May/June 2018

86. Which of the following statements is incorrect regarding forward rate calculation?
(A) A discount is always deducted from the spot rate in the case of direct quotations.
(B) If forward points are 15-18, the base currency is at a discount.
(C) A premium is always added to the spot rate in the case of direct quotations.
(D) Forward rates are typically quoted by stating the spot rate and forward differentials separately.

Ans :

(B) If forward points are 15-18, the base currency is at a discount.
If forward points are quoted in ascending order (the first number is lower than the second, e.g., 15-18), it signifies that the base currency is at a premium, not a discount. The premium points are then added to the spot rate to determine the outright forward rate.

Oct/Nov 2014

87. An export customer has a bill for £ 100,000. The bank's cross rate calculation results in £ 1 = ₹95.2028. How many rupees will the customer receive?
(A) ₹10,000,000
(B) ₹952,028
(C) ₹9,250,820
(D) ₹9,520,280

Ans :

(D) ₹9,520,280
The bank is purchasing the £ 100,000 bill from the customer at the derived buying rate of ₹95.2028 per pound. The total amount in rupees to be paid to the customer is the foreign currency amount multiplied by the exchange rate:
100,000 × 95.2028 = ₹9,520,280.

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May/June 2021

88. Statement (I): The settlement date for a transaction at the 'Ready' rate is the same day as the deal.
Statement (II): The settlement date for a transaction at the 'Spot' rate is the next working day after the deal.
Which of the following is correct?
(A) Both Statement (I) and Statement (II) are correct.
(B) Statement (I) is correct, but Statement (II) is incorrect.
(C) Statement (I) is incorrect, but Statement (II) is correct.
(D) Both Statement (I) and Statement (II) are incorrect.

Ans :

(B) Statement (I) is correct, but Statement (II) is incorrect.
Statement (I) is correct; 'Ready' or 'Cash' rate transactions settle on the same day (T+0). Statement (II) is incorrect; 'Spot' rate transactions settle on the second working day (T+2) after the deal, not the next working day. The rate for the next working day is the 'TOM' rate.

Oct/Nov 2010

89. A trader observes that the interest rate on Euros is 3% p.a. and on US Dollars is 6% p.a. The spot rate is € 1 = $1.5000. The trader borrows € 100 for

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Reason (R) correctly defines a premium: the currency is more expensive for forward delivery. Assertion (A) correctly states the mechanical application of this concept in direct quotes. Because the currency is costlier, the premium points must be added to the spot price to arrive at the higher forward price. Thus, (R) explains (A).

May/June 2011

80. Identify the incorrect pair from the following options.
(A) LERMS : Liberalised Exchange Rate Management System
(B) Swap Rate : Another name for Spot Rate
(C) Spot Rate : Settlement on T+2
(D) Arbitrage : Risk-free profit from offsetting transactions

Ans :

(B) Swap Rate : Another name for Spot Rate
The 'Swap Rate' is another term for the 'Forward Differential' or 'Forward Points', which is the difference between the forward rate and the spot rate. It is not another name for the spot rate itself. The other pairs correctly define the acronym LERMS, the settlement for a spot rate, and the concept of arbitrage.

Oct/Nov 2020

81. Which of the following statements about the Indian Forex Market is correct?
(A) At present, the forces of demand and supply in the local interbank market primarily drive the exchange rate.
(B) Exchange rates are currently determined by the RBI, which fixes them daily within a predefined narrow band.
(C) Prior to LERMS, rates were determined freely by market demand and supply without central bank intervention.
(D) The country currently has no restrictions whatsoever on the free flow of capital into or out of its borders.

Ans :

(A) At present, the forces of demand and supply in the local interbank market primarily drive the exchange rate.
After the introduction of the Liberalised Exchange Rate Management System (LERMS), the primary determinant of the Indian Rupee's exchange rate became the market mechanism. The interaction of demand and supply for currencies within the local interbank market is what currently drives rate movements, not direct RBI fixing.

May/June 2013

82. If the Spot rate is \$1 = ₹75.00 and the 1-month forward rate is \$1 = ₹75.10, the forward differential is:
(A) 10 points discount
(B) 7510 points premium
(C) 7500 points discount
(D) 10 points premium

Ans :

(D) 10 points premium
The forward rate (₹75.10) is higher than the spot rate (₹75.00), so the US dollar is at a premium. The forward differential is the difference, which is ₹75.10 - ₹75.00 = ₹0.10. In market parlance, this is referred to as 10 points or 10 paise.

Oct/Nov 2016

83. The process of calculating the INR/GBP rate using the known USD/INR and USD/GBP rates is an application of:
(A) The Value Date rule
(B) The Arbitrage principle
(C) The Chain Rule or Cross Rate calculation
(D) The Premium/Discount rule

Ans :

(C) The Chain Rule or Cross Rate calculation
When a direct exchange rate between two currencies (like INR and GBP) is not available, the rate is derived by using a common third currency (like USD). This method of linking rates through an intermediate currency is known as calculating a cross rate, which can be formalized using the Chain Rule.

May/June 2016

84. A transaction with a value date on the second working day after the deal date is known as a:
(A) Cash transaction
(B) Tom transaction
(C) Forward transaction
(D) Spot transaction

Ans :

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domestically.
(C) To facilitate the immediate settlement of international trade payments and receipts.
(D) To eliminate the risk of adverse exchange rate fluctuations for a future transaction.

Ans :

(D) To eliminate the risk of adverse exchange rate fluctuations for a future transaction.
The main function of a forward contract is risk management, also known as hedging. It allows an importer or exporter to lock in an exchange rate for a future date, thereby protecting them from potential losses that could arise if the exchange rate moves unfavorably before the payment or receipt date.

Oct/Nov 2020

95. I. The Indian forex market completely follows the international trend.
II. LERMS led to RBI fixing both buying and selling rates.
III. The Indian forex rate is currently driven by local interbank demand and supply.
Which of the statements is/are correct?
(A) Only III
(B) Only I and II
(C) Only II and III
(D) I, II, and III

Ans :

(A) Only III
Statement I is incorrect; due to capital controls, the Indian market does not always follow international trends. Statement II is incorrect; LERMS led to market-determined rates, while RBI fixing was the pre-LERMS system. Statement III is correct; post-LERMS, local interbank market forces of demand and supply drive the exchange rate.

May/June 2011

96. If the Spot € 1 = $1.2180/1.2190 and 3-month forward points are 41-49, what is the 3-month outright forward quote for € 1?
(A) $1.2139 / 1.2141
(B) $1.2221 / 1.2239
(C) $1.2229 / 1.2231
(D) $1.2131 / 1.2149

Ans :

(B) $1.2221 / 1.2239
The points 41-49 are in ascending order, indicating a premium. The premium is added. Outright Bid = Spot Bid + Bid Points = 1.2180 + 0.0041 = 1.2221. Outright Offer = Spot Offer + Offer Points = 1.2190 + 0.0049 = 1.2239. The full quote is $1.2221 / 1.2239.

Oct/Nov 2012

97. If the Spot € 1 = $1.2180/1.2190 and 3-month forward points are 33-25, what is the 3-month outright forward quote for € 1?
(A) $1.2213 / 1.2215
(B) $1.2147 / 1.2165
(C) $1.2155 / 1.2157
(D) $1.2147 / 1.2155

Ans :

(B) $1.2147 / 1.2165
The points 33-25 are in descending order, indicating a discount. The discount is subtracted. Outright Bid = Spot Bid - Bid Points = 1.2180 - 0.0033 = 1.2147. Outright Offer = Spot Offer - Offer Points = 1.2190 - 0.0025 = 1.2165. The full quote is $1.2147 / 1.2165.

May/June 2015

98. "The exchange from one currency for another is, mostly, put through by the banks by means of bookkeeping entries carried out in the two centres concerned."
This statement implies that the foreign exchange mechanism primarily relies on:
(A) The correspondent banking system.
(B) Physical shipment of gold between central banks.
(C) The use of cryptocurrency for settlement.
(D) Direct government-to-government fund transfers.

Ans :

(A) The correspondent banking system.
The "bookkeeping entries carried out in the two centres" refers to the debits and credits made in accounts that banks hold with each other across different countries. This network of accounts is the essence of the correspondent banking system, which facilitates international payments and currency exchange without the physical movement of cash.

Oct/Nov 2007

99. A bank is asked to calculate the 60-day forward points for a currency pair. The spot rate is 1.3500,

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one year, converts to USD, and deposits it. What is the total amount of US Dollars the trader will have after one year?
(A) $150
(B) $153
(C) $159
(D) $156

Ans :

(C) $159
The trader converts € 100 to $150 at the spot rate. This $150 is deposited for one year at 6% interest. The interest earned is 150 6% = 9. The total amount of US Dollars at the end of the year is the principal plus interest: 150 + 9 = $159.

May/June 2013

90. Following the previous scenario, the trader owes € 103 at the end of the year. To prevent arbitrage, the $159 held by the trader must be equivalent to € 103. What is the implied one-year forward exchange rate?
(A) € 1 = $1.5436
(B) € 1 = $1.5000
(C) € 1 = $1.5900
(D) € 1 = $1.5145

Ans :

(A) € 1 = $1.5436
The no-arbitrage condition requires that the future values are equal when converted at the forward rate. Therefore, € 103 must equal 159. To find the rate for € 1, we divide the US dollar amount by the Euro amount: Rate = 159 / 103 ≈ 1.5436. So, the forward rate is € 1 = $1.5436.

Oct/Nov 2021

91. "In case of direct quotations, a premium is always added, i.e. added to both buying and selling side... a discount is always deducted, i.e. deducted both from the buying and selling side."
If the spot rate is 1.1000/1.1010 and the currency is at a discount, the outright forward spread will be:
(A) Narrower than the spot spread.
(B) The same as the spot spread.
(C) Zero.
(D) Wider than the spot spread.

Ans :

(D) Wider than the spot spread.
When a currency is at a discount, a larger number of points is subtracted from the bid rate and a smaller number of points from the offer rate. This action pushes the bid rate down more than the offer rate, resulting in the spread between the forward bid and offer rates becoming wider than the original spot spread.

May/June 2024

92. Identify the correct chronological order of settlement dates, from earliest to latest.
(A) Spot, Tom, Cash, Forward
(B) Cash, Tom, Spot, Forward
(C) Tom, Cash, Forward, Spot
(D) Cash, Spot, Tom, Forward

Ans :

(B) Cash, Tom, Spot, Forward
The correct chronological order based on settlement time is: Cash/Ready (T+0, same day), followed by Tom (T+1, next working day), then Spot (T+2, second working day), and finally Forward (any date after T+2). This sequence represents an increasing time lag between the deal date and the value date.

Oct/Nov 2016

93. If a bank quotes US$/INR as 74.50/60, what does this mean?
(A) The bank buys US at ₹74.60 and sells at ₹74.50.
(B) The customer can buy US at ₹74.50 and sell at ₹74.60.
(C) The bank buys US at ₹74.50 and sells at ₹74.60.
(D) The rate is applicable for both buying and selling at ₹74.55.

Ans :

(C) The bank buys US at ₹74.50 and sells at ₹74.60.
A two-way quote always lists the bank's buying rate (bid) first and its selling rate (offer/ask) second. The bank will always buy the base currency (US$) at the lower price (₹74.50) and sell it at the higher price (₹74.60) to make a profit from the spread.

May/June 2009

94. What is the primary purpose of a forward exchange contract?
(A) To speculate on very short-term currency movements within a single trading day.
(B) To earn a higher rate of interest on foreign currency holdings than is available

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May/June 2006

104. Which of the following is NOT a type of exchange rate based on the value date?
(A) Cross Rate
(B) Spot Rate
(C) Tom Rate
(D) Cash Rate

Ans :

(A) Cross Rate
Cash, Tom, Spot, and Forward rates are all defined based on their settlement or value date (T+0, T+1, T+2, and >T+2, respectively). A Cross Rate, however, is not defined by its value date but by its method of calculation, where the rate between two currencies is derived via a third currency.

Oct/Nov 2013

105. A currency is said to be at a discount in the forward market if it is:
(A) Costlier to acquire for a future value date.
(B) Completely unavailable for future delivery.
(C) Priced exactly the same as the spot rate.
(D) Cheaper to acquire for a future value date.

Ans :

(D) Cheaper to acquire for a future value date.
A currency is at a discount when its forward price is lower than its spot price. This means it is cheaper to buy or sell that currency for a future settlement date compared to the immediate spot settlement. In direct quotes, this discount is subtracted from the spot rate to determine the forward rate.

May/June 2008

106. A bank quotes a spot rate for EUR/USD as 1.0850/60. The 1-month forward points are 10-12. An importer wishes to buy Euros 1 month forward. What rate will the bank quote?
(A) 1.0860
(B) 1.0872
(C) 1.0848
(D) 1.0862

Ans :

(B) 1.0872
The importer is buying Euros, so the bank's offer rate is used. The spot offer is 1.0860. The forward points (10-12) are ascending, indicating a premium, so they are added. The offer side points are 12. The outright forward offer rate is $1.0860 + 0.0012 = 1.0872.

Oct/Nov 2015

107. **Assertion (A) :** In a market with efficient communication, arbitrage opportunities in exchange rates are very rare.
Reason (R) : Any price discrepancies between markets are quickly eliminated by traders executing offsetting transactions.
(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
(B) Both (A) and (R) are true but (R) is not the correct explanation of (A).
(C) (A) is true but (R) is false.
(D) (A) is false but (R) is true.

Ans :

(A) Both (A) and (R) are true and (R) is the correct explanation of (A).
Assertion (A) is a correct statement about modern forex markets. Reason (R) accurately explains why this is the case. The speed of information flow allows traders to spot and act on price differences almost instantly, and their collective actions bring prices back into alignment, thus eliminating the arbitrage opportunity.

May/June 2007

108. The formula to calculate annualized interest rate differential from forward points requires all of the following inputs EXCEPT:
(A) Forward points
(B) Outright forward rate
(C) Spot rate
(D) Forward period

Ans :

(B) Outright forward rate
The formula is Interest Rate Differential = (Forward points No. of days in year 100) / (Spot rate Forward period). This calculation directly uses the forward points, spot rate, and forward period. The outright forward rate is the result of applying points to the spot rate, not an input to this specific formula.

Oct/Nov 2024

109. If the three-month forward USD is at a premium against the INR in a direct quote, it means:
(A) An importer buying USD three months forward will pay fewer rupees than at spot.
(B) The three-month forward rate (INR/USD) is

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(C) 1.2160 - 1.2170
(D) 1.2170 - 1.2154

Ans :

(A) 1.2154 - 1.2170
The 2-month outright bid rate was calculated as 1.2154, and the 2-month outright offer rate was calculated as 1.2170. Combining these gives the full two-way outright forward quote, which is expressed as the bid rate followed by the offer rate: $1.2154 - 1.2170.

Oct/Nov 2013

71. What does it mean if a forward rate is 'At Par'?
(A) The forward rate is significantly higher than the spot rate.
(B) The spot rate and the forward rate are the same.
(C) The forward rate is significantly lower than the spot rate.
(D) The forward transaction has been cancelled.

Ans :

(B) The spot rate and the forward rate are the same.
A forward rate is described as being 'at par' when it is exactly the same as the corresponding spot rate. This situation implies that there is no forward premium or discount on the currency for that specific forward period. In this case, the forward differential or forward points would be zero.

May/June 2008

72. In the case of direct rates, when is the base currency considered to be at a premium?
(A) When the forward rate is less than the spot rate.
(B) When the forward rate is equal to the spot rate.
(C) When the forward rate is quoted with a wider spread.
(D) When the forward rate is more than the spot rate.

Ans :

(D) When the forward rate is more than the spot rate.
For direct quotations, a simple comparison between the forward and spot rates determines the premium or discount. If the outright forward rate is higher (more) than the spot rate, it means the base currency is more expensive in the future, and thus it is considered to be at a premium.

Oct/Nov 2015

73. In the case of direct rates, under what condition is the base currency said to be at a discount?
(A) When the forward rate is less than the spot rate.
(B) When the forward rate is more than the spot rate.
(C) When the forward rate is the same as the spot rate.
(D) When the forward rate is not quoted.

Ans :

(A) When the forward rate is less than the spot rate.
When using direct quotations, the base currency is determined to be at a discount if its outright forward rate is lower (less) than the current spot rate. This indicates that the currency is cheaper to purchase for future delivery compared to immediate settlement, reflecting a negative cost of carry.

May/June 2024

74. Which of the following correctly identifies a pair of terms and their definitions?
(A) Direct Quote: The foreign currency price of one unit of the home currency.
(B) Cross Rate: The average of the bid and ask price for a currency pair.
(C) TOM Rate: Settlement on the next working day after the deal is made.
(D) Value Date: The date on which a foreign exchange deal is negotiated.

Ans :

(C) TOM Rate: Settlement on the next working day after the deal is made.
The TOM (tomorrow) rate is correctly defined as the exchange rate for a transaction where settlement occurs on the next working day. A direct quote is the home currency price of a foreign currency unit. A cross rate is derived via a third currency. A value date is the settlement date, not the negotiation date.

Oct/Nov 2008

75. Identify the incorrect statement regarding foreign exchange fundamentals.
(A) The useful possession of a currency is easily transferable and valid in any country.

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The relationship between premium and discount for a currency pair is always reciprocal. If one currency (Euro) is cheaper in the forward market (at a discount), the other currency (US Dollar) must be more expensive in the forward market (at a premium) relative to the first. Both cannot be at a discount simultaneously.

May/June 2014

114. A bank is quoting GBP/USD. The spot rate is 1.2500/10. The 2-month forward points are 40-35. An exporter needs to sell GBP 2 months forward. What is the outright rate the bank will offer?
(A) 1.2465
(B) 1.2475
(C) 1.2540
(D) 1.2460

Ans :

(D) 1.2460
The exporter is selling GBP, so the bank's bid rate applies (1.2500). The forward points 40-35 are in descending order, indicating a discount, so they are subtracted. The higher point (40) is subtracted from the bid rate. The outright bid rate is 1.2500 - 0.0040 = 1.2460.

Oct/Nov 2006

115. The difference of 150 points between a spot rate of 1.2180 and a 3-month forward rate of 1.2330 for the US$/Euro pair are referred to as:
(A) Forward points
(B) Spot points
(C) Arbitrage points
(D) Interest points

Ans :

(A) Forward points
The difference between a spot exchange rate and a forward exchange rate is known as the forward points, forward differential, or swap points. These points represent the market's adjustment for factors like the interest rate differential between the two currencies over the specified forward period.

May/June 2025

116. Statement (I): If forward points are quoted as 25-30, the base currency is at a premium.
Statement (II): A premium is always subtracted from the spot rate in a direct quotation.
Which of the following is correct?
(A) Both Statement (I) and Statement (II) are correct.
(B) Statement (I) is correct, but Statement (II) is incorrect.
(C) Statement (I) is incorrect, but Statement (II) is correct.
(D) Both Statement (I) and Statement (II) are incorrect.

Ans :

(B) Statement (I) is correct, but Statement (II) is incorrect.
Statement (I) is correct. When forward points are in ascending order (25-30), the base currency is at a premium. Statement (II) is incorrect. In a direct quotation, a premium is always added to the spot rate to reflect the higher forward cost, not subtracted. A discount is subtracted.

Oct/Nov 2019

117. Which statement correctly describes the components of a forward rate?
(A) It is composed of the TOM rate and a separately calculated risk adjustment factor.
(B) It is composed of the cash rate and the central bank's official inflation forecast.
(C) It is composed of the previous day's closing spot rate and a market volatility index.
(D) It is composed of the spot rate and an adjustment for interest rate differentials.

Ans :

(D) It is composed of the spot rate and an adjustment for interest rate differentials.
A forward rate is not an independent quote but is derived from the current spot rate. The spot rate is adjusted by the forward points, which primarily reflect the interest rate differential between the two currencies for the duration of the forward period. This adjustment accounts for the time value of money.

May/June 2010

118. What is the fundamental logic that links interest rates to forward exchange rates?
(A) The trade-off between interest earned on one currency and the opportunity cost of not earning interest on another.
(B) The political need to balance trade deficits between two countries over the long term.
(C) The regulatory requirement set by the Bank for International Settlements (BIS) for all member banks.
(D) The historical statistical correlation between

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deal.

(D) The type of financial institution conducting the transaction.

Ans :

(A) The settlement date (value date) of the transaction.

The primary distinction between spot and forward transactions lies in their value date. A spot transaction settles on the second business day after the deal (T+2), representing the current market price. A forward transaction settles on any date after the spot date, at a price agreed upon today for future delivery.

Oct/Nov 2014

129. If the USD is at a premium against the INR for 3 months forward, what does this imply for the INR?

(A) The INR is also at a premium against the USD.

(B) The INR is at par with the USD.

(C) The INR is at a discount against the USD.

(D) The INR/USD exchange rate is fixed.

Ans :

(C) The INR is at a discount against the USD.

The relationship is reciprocal. If one currency (USD) is costlier in the forward market (premium), the other currency (INR) must be cheaper in the forward market (discount) relative to the first. An investor would have to pay more INR to get a USD forward, which is the same as saying one USD buys more INR forward.

May/June 2021

130. I. A direct quote is home currency per unit of foreign currency.

II. A 'Tom' transaction settles on T+1.

III. A 'Spot' transaction settles on T+2.

IV. If forward points are 40-50, the base currency is at a premium.

V. If the base currency is at a premium, points are subtracted from the spot rate.

Which combination of statements is correct?

(A) I, II, III, IV, V

(B) I, II, III, IV only

(C) I, II, V only

(D) I, III, IV only

Ans :

(B) I, II, III, IV only

Statements I, II, III, and IV are all correct definitions and rules. Statement V is incorrect. If the base currency is at a premium, the forward points are added to the spot rate in a direct quotation to reflect the higher forward cost, not subtracted. Subtraction applies when the currency is at a discount.

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(C) At par
(D) At a cross

Ans :

(C) At par
When the forward exchange rate is exactly the same as the spot exchange rate, it indicates there is no premium or discount. This situation is referred to as the forward rate being 'at par' with the spot rate. The forward points or swap rate in this case would be zero.

May/June 2023

124. I. They are determined by interest rate differentials.
II. They are determined by market expectations.
III. They are determined by supply and demand for the settlement date.
IV. They are always quoted in ascending order.
Which combination of statements is correct regarding forward points?
(A) I, II, III, and IV
(B) I, II, and III only
(C) I and IV only
(D) II and III only

Ans :

(B) I, II, and III only
Statements I, II, and III list the three primary factors that determine forward points: interest rate differentials (the most dominant), market view/expectations, and currency supply/demand for the value date. Statement IV is incorrect; forward points can be quoted in ascending order (premium) or descending order (discount).

Oct/Nov 2018

125. An indirect quote for the Euro in London would be expressed as:
(A) EUR per 1 USD
(B) GBP per 1 EUR
(C) EUR per 1 GBP
(D) USD per 1 GBP

Ans :

(C) EUR per 1 GBP
An indirect quote is the foreign currency price of one unit of the home currency. For a person or bank in London, the home currency is the Pound Sterling (GBP). Therefore, an indirect quote for the Euro (EUR) would be expressed as the number of Euros per one Pound Sterling.

May/June 2016

126. "We can say that if in forward points the first figure is lower than the second figure, the base currency is at a premium in forwards."
Given a quote where 1-month forward points are 20-25, what action is taken to calculate the outright forward rate in a direct quotation?
(A) The points are subtracted from the spot rate.
(B) The points are added to the spot rate.
(C) The average of the points is added to the spot rate.
(D) The points are ignored, and the spot rate is used.

Ans :

(B) The points are added to the spot rate.
According to the rule provided, forward points of 20-25 (first figure lower than the second) indicate that the base currency is at a premium. In the case of direct quotations, a premium is always added to the spot rate to calculate the outright forward rate, reflecting the higher future cost of the currency.

Oct/Nov 2025

127. A forex dealer provides the following quote for JPY/USD: Spot 110.10/20. The 1-month forward points are 15-12. A client wants to sell USD 1 million for 1-month forward delivery. How many JPY will the client receive?
(A) 109,950,000 JPY
(B) 110,220,000 JPY
(C) 110,080,000 JPY
(D) 109,980,000 JPY

Ans :

(A) 109,950,000 JPY
The client is selling USD (the base currency), so the bank's bid rate applies. Spot bid is 110.10. The points 15-12 are descending, indicating a discount, so they are subtracted. The higher point (15) is subtracted from the bid: 110.10 - 0.15 = 109.95. The client will receive 1,000,000 109.95 = 109,950,000 JPY.

May/June 2018

128. What is the key difference between a Spot transaction and a Forward transaction?
(A) The settlement date (value date) of the transaction.
(B) The specific pair of currencies being exchanged.
(C) The total monetary amount involved in the

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inflation rates and exchange rate movements.

Ans :

(A) The trade-off between interest earned on one currency and the opportunity cost of not earning interest on another.
The core principle is Interest Rate Parity. An investor should be indifferent between investing in a domestic asset or investing in a foreign asset after hedging the currency risk. The forward rate adjusts to offset the interest rate differential, balancing the interest earned on one currency with the opportunity cost of forgoing interest on the other.

Oct/Nov 2022

119. "The formula for calculating the interest rate differential from the forward points is as under: Interest rate differential = (Forward points No. of days in the year 100) / (Spot rate Forward period)" According to this formula, if the spot rate increases while all other variables remain constant, what will be the effect on the calculated interest rate differential?
(A) It will increase.
(B) It will remain unchanged.
(C) It will decrease.
(D) It will become zero.

Ans :

(C) It will decrease.
In the provided formula, the 'Spot rate' is in the denominator. Therefore, there is an inverse relationship between the spot rate and the calculated interest rate differential. If the spot rate increases and all other factors are held constant, the value of the entire fraction will decrease.

May/June 2005

120. An Indian importer has a payment of $50,000 due in 3 months. The spot USD/INR rate is ₹74.8450. The 3-month forward rate is ₹74.8725. The importer decides to book a forward contract. What will be the total cost in INR?
(A) ₹3,743,625
(B) ₹3,742,250
(C) ₹3,740,875
(D) ₹3,700,000

Ans :

(A) ₹3,743,625
The importer needs to buy US dollars for a future date. The applicable rate is the 3-month forward rate of ₹74.8725 per US dollar. The total cost for the importer will be the US dollar amount multiplied by this forward rate: 50,000 74.8725 = ₹3,743,625.

Oct/Nov 2017

121. What happens to the bid-ask spread when forward points for a discount (e.g., 26-20) are applied to a spot rate?
(A) The spread becomes narrower.
(B) The spread remains the same.
(C) The spread becomes wider.
(D) The spread becomes negative.

Ans :

(C) The spread becomes wider.
For a discount, the larger point value (26) is subtracted from the bid, and the smaller point value (20) is subtracted from the offer. Subtracting a larger number from the bid and a smaller number from the offer pushes the two rates further apart, thus widening the bid-ask spread compared to the spot spread.

May/June 2012

122. Which of the following is the most accurate description of the 'Swap Rate' in forex?
(A) The specific interest rate applied on a cross-currency interest rate swap.
(B) Another term for the forward differential or forward points.
(C) Another market term for the current spot exchange rate.
(D) The commission or fee charged by a broker for executing a forex transaction.

Ans :

(B) Another term for the forward differential or forward points.
In the context of foreign exchange arithmetic, the 'Swap Rate' is a market term used interchangeably with 'forward points' or 'forward differential'. It represents the difference between the forward rate and the spot rate and is a key component in pricing forex swaps and outright forward contracts.

Oct/Nov 2009

123. If the spot rate and the forward rate for a currency are identical, the forward differential is zero, and the forward rate is said to be:
(A) At a premium
(B) At a discount

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